TRANSCRIPT OF RECORD

Supreme Court of the United States

OCTOBER TERM, 1942

No. 452

CORN EXCHANGE NATIONAL BANK AND TRUST COMPANY, PHILADELPHIA, AND EDWARD C. DEARDEN, SR., PETITIONERS,

vs.

NORMAN KLAUDER, TRUSTEE OF QUAKER CITY SHEET METAL CO., BANKRUPT

ON WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE THIRD CIRCUIT

PETITION FOR CERTIORARI FILED OCTOBER 12, 1942.

CERTIORARI GRANTED NOVEMBER 9, 1942.

SUPREME COURT OF THE UNITED STATES

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INDEX

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—2302

[fol. 1]

IN THE DISTRICT COURT OF THE UNITED STATES FOR THE EASTERN DISTRICT OF PENNSYLVANIA

No. 21312. In Bankruptcy

In the Matter of QUAKER CITY SHEET METAL COMPANY, Bankrupt

RELEVANT DOCKET ENTRIES

April 18, 1940. Petition filed. Subpoena exit—returnable April 29, 1940.

May 7, 1940. Adjudication of bankruptcy, filed.

June 7, 1940. Bond of Norman Klauder as Trustee in $5000, with New Amsterdam Casualty Co. as surety, approved and filed.

April 29, 1941. Certificate for Review re claim of Edward C. Dearden, Sr., filed.

April 29, 1941. Certificate for Review, re claim of Corn Exchange Nat. Bank and Trust Co., filed.

May 22, 1941. Praecipe to place on argument list Certificate for review re claim of Edward C. Dearden, Sr., filed.

May 22, 1941. Praecipe to place on argument list Certificate for Review re claim of Corn Exchange Natl. Bank & Trust Co., filed.

June 16, 1941. Hearing on certificate for review re claim of Corn Exchange National Bank.

June 16, 1941. Hearing on certificate for review re claim of Edward C. Deardon, Sr.

Sept. 17, 1941. Memorandum affirming orders of Referee re claim of Corn Exchange National Bank and Trust Co., and re Claim of Edward C. Dearden, Sr., filed.

Nov. 10, 1941. Final decree affirming orders of Referee re claim of Corn Exchange National Bank and Trust Co. and re Claim of Edward C. Dearden, Sr., filed.

(Noted 11/10/41—Copies sent to Counsel.)

[fols. 2-4] Nov. 25, 1941. Notice of appeal filed. (11/26/41 Copy to W. F. Mikell and L. H. Van Dusen).

Nov. 25, 1941. Copy of Clerk's notice of appeal filed.

Dec. 10, 1941. Designation of record on appeal filed.

Dec. 10, 1941. Designation by appellee, Edward C. Dearden, Sr., of additional portion of record to be included in record on appeal filed.

Dec. 10, 1941. Designation by appellee, Corn Exchange National Bank and Trust Co., of additional portion of record to be included in record on appeal filed.

[fol. 5] IN UNITED STATES DISTRICT COURT

[Title omitted]

PETITION FOR RECLAMATION OF $1550

To the Honorable the Judges of the said Court:

Edward C. Dearden, Sr., petitioner herein, seeks to recover the sum of $1550 in the hands of Norman Klauder and B. Mitchell Simpson, Receivers in Bankruptcy of Quaker City Sheet Metal Company and/or its Trustee in Bankruptcy, Norman Klauder, and in connection therewith Respectfully Represents:

1. The involuntary petition in bankruptcy in this case was filed on or about April 18, 1940 against Quaker City Sheet Metal Company (hereinafter called the Company).

2. Prior to the institution of the instant proceedings and on or about April 12, 1940 your petitioner, Edward C. Dearden, Sr., at the instance of Quaker City Sheet Metal Company and its Creditors' Committee, hereinafter referred to, loaned to Company the sum of $1550 in consideration of the receipt by your petitioner of a certain assignment by said Company to your petitioner, a true and correct copy of which is hereto attached, marked "Exhibit A" and made a part hereof.

3. The circumstances under which the aforesaid loan of [fol. 6] $1550 made by your petitioner to said Company was made and said assignment marked "Exhibit A" hereof was executed and delivered by said Company to your Petitioner are as follows:

4. The Company was engaged in the business of fabrication, erection and sale of all types of sheet metal work. During the Spring of 1938 the Company became in financial

difficulties and at the instance of its larger creditors there was formed a Creditors' Committee to represent creditors joining in the creditors' agreement and to supervise the business of the Company in the interest of the creditors. The Committee, consisting of L. Norris Hall, V. W. Hayden, B. M. Simpson and Norman Klauder, was formed under the terms of a certain written agreement dated April 27, 1938 between the said Committee, the Company and such of its creditors as joined in the agreement. A true and correct copy of the said creditors' agreement is hereto attached, marked "Exhibit B" and made a part hereof. Substantially all of the then important creditors of the Company signed the said creditors' agreement and thereby appointed the said Committee as their agent in connection with the affairs of the Company. The creditors who signed the said agreement, and whose claims aggregate approximately 80% of the present claims of creditors against the bankrupt, excluding the secured claim of Corn Exchange National Bank and Trust Company, are as follows: Apollo Steel Company, Chase Brass & Copper Co., L. Norris Hall, Inc., Wheeling Corrugating Co. and William A. Simpson & Son.

5. The term of the said creditors' agreement (Exhibit B hereof) was, by mutual consent of the parties thereto, extended from time to time to August 27, 1940.

[fol. 7] 6. The said Creditors' Committee, functioning as a representative of the aforesaid creditors, supervised and was familiar with all of the activities of the Company from the time of its inception until the date of bankruptcy. Shortly prior to April 12, 1940 the Company, having exhausted its cash and being unable to meet its current payroll, was faced with the necessity of raising cash for its current payroll; accordingly, the Creditors' Committee urged the President of the Company to secure the aforesaid loan of $1550. from your petitioner for the purpose of meeting the current wages payable to its employees constituting its then current payroll and suggested through the attorneys for the said Creditors' Committee, Jenkins, Bennett & Libby, Esqs., that the said loan be obtained and secured by an assignment of a certain contract between Company and York Ice Machinery Corporation, dated March 12, 1940, evidenced by York Ice Machinery Corporation's purchase order No. 89113 of March 12, 1940.

7. The Company, under the supervision of and at the instigation of the said Creditors' Committee, obtained the said loan of $1550. from your petitioner in consideration of the execution and delivery by the Company to him of the aforesaid assignment of said contract with York Ice Machinery Corporation and the proceeds thereof, as more particularly set forth in the said assignment (Exhibit A hereof).

8. The said assignment was prepared by counsel for the Creditors' Committee, Jenkins, Bennett & Libby, Esqs. and executed and delivered as therein recited.

9. Your petitioner has received no payment of any sort on account of the said loan nor has he received any of the proceeds due by reason of performance of the said contract with York Ice Machinery Corporation by the Company.

[fol. 8] 10. On or about May 4, 1940, William E. Mikell, Jr., Esq., as attorney for your petitioner, notified Jenkins, Bennett & Libby, Esqs., attorneys for the Receivers of the bankrupt, of the claim of your petitioner to the proceeds of the said contract of York Ice Machinery Corporation. A true and correct copy of said notice is hereto attached, marked "Exhibit C" and made a part hereof. At that time the said contract with York Ice Machinery Corporation had been partially performed by the Company prior to its bankruptcy. The Receivers had no funds with which to complete the contract.

11. On June 18, 1940, when the said Trustee in Bankruptcy had been appointed, said attorney for your petitioner notified the Trustee of the said assignment and the claim of your petitioner to the proceeds of the said contract as aforesaid. A true and correct copy of the said notice is hereto attached, marked "Exhibit D" and made a part hereof.

12. Your petitioner has been advised and therefore avers that on or prior to August 20, 1940 Norman Klauder as Trustee in Bankruptcy of the above named bankrupt, received from York Ice Machinery Corporation on account of the said contract the sum of $1591., which he is holding subject to the disposition of this claim by your petitioner to the proceeds of the said contract so received. Your petitioner is informed and therefore avers that the full contract

price set forth in said contract between the Company and York Ice Machinery Corporation was $2711. Your petitioner is informed by the Trustee and therefore avers that the said Trustee agreed with York Ice Machinery Corporation for a credit to York Ice Machinery Corporation of $1120. as the cost of completion by York Ice Machinery Corporation of the aforesaid contract. The said sum of $1591 in the hands of the Trustee as aforesaid represents [fol. 9] the balance paid by York Ice Machinery Corporation to the Trustee in Bankruptcy for partial performance by the Company of said contract.

13. Your petitioner is informed, believes and therefore avers that all of the said sum of $1550. loaned by him to the Company under the circumstances aforesaid, was in fact used for the payment of current wages by the Company to its employees.

Wherefore your petitioner prays that an order be entered directing Norman Klauder and B. Mitchell Simpson, as Receivers in Bankruptcy of Quaker City Sheet Metal Company, and/or Norman Klauder as Trustee of the aforesaid bankrupt, to turn over to and pay to your petitioner the said sum of $1550. which your petitioner claims to own by reason of the aforesaid assignment and the circumstances heretofore recited.

And your petitioner will ever pray.

Edward C. Dearden.

Duly sworn to by Edward C. Dearden, Sr. Jurat omitted in printing.

[fol. 10] EXHIBIT "A" TO PETITION

Know All Men by These Presents, That whereas the York Ice Machinery Corporation has entered into an agreement with the Quaker City Sheet Metal Company for the installation of certain materials and equipment to be manufactured by the Quaker City Sheet Metal Company, said agreement being dated March 12, 1940, and further evidenced by purchase order No. 89113 of same date,

And whereas Edward C. Dearden, Sr. has advanced to the Quaker City Sheet Metal Company certain sums of money, to wit One Thousand Five Hundred Fifty Dollars ($1,550.00) under date of April 12, 1940.

Now, therefore, for and in consideration of the monies so advanced by Edward C. Dearden, Sr. as well as for other good and valuable consideration and in order to better secure the repayment of the said money to Edward C. Dearden, Sr.,

The Quaker City Sheet Metal Company has assigned, set over, transferred and conveyed, and by these presents does assign, transfer, set over and convey to said Edward C. Dearden, Sr., his heirs, administrators, executors and assigns, any and all of its right, title and interest in and to the said agreement with York Ice Machinery Corporation hereinabove referred to and any monies now due, or hereafter to become due, to the Quaker City Sheet Metal Company by reason of the said agreement and/or purchase order, together with the right to demand, sue for, collect and receive the same, and to apply any sums received thereunder to the payment of the said indebtedness of the Quaker City Sheet Metal Company to the said Edward C. Dearden, Sr., together with any reasonable expense incurred for the collection thereof provided, however, that any surplus received over and above the amount necessary for the repayment of the said Edward C. Dearden, Sr. shall be refunded to the said Quaker City Sheet Metal Company.

[fol. 11] In Witness Whereof, the said Quaker City Sheet Metal Company has caused these presents to be executed by E. C. Dearden, Jr., its President, duly attested by Robert M. Carrigan, its Secretary, and the corporate seal affixed hereto this 12th day of April, 1940.

Quaker City Sheet Metal Company, by E. C. Dearden, Jr., President. (Corporate Seal.)

Attest: Robert M. Carrigan, Secretary.

[fol. 12] EXHIBIT "B" TO PETITION

Agreement made as of April 27th, 1938, by and between Quaker City Sheet Metal Co., a Pennsylvania corporation, party of the first part (hereinafter called Debtor), L. Norris Hall (of L. Norris Hall, Inc.), V. W. Heyden (of Chase Brass & Copper Co.), W. W. Keefer (of Apollo Steel Company), B. M. Simpson (of W. A. Simpson & Son), and Norman Klauder, parties of the second part (hereinafter called Committee), and Creditors of Debtor signatory hereto, par-

ties of the third part (hereinafter jointly and severally called Creditors), Witnesseth:

Whereas Debtor is unable to meet its obligations in the ordinary course of business, and desires to obtain from Creditors, and Creditors are willing to grant, an extension of time for the payment of their respective claims;

Now, Therefore, in consideration of the obligations imposed upon and benefits to accrue to Company and Creditors respectively, and in consideration of the mutual promises of the parties hereto, the several parties hereto (each for himself or for itself and not for any of the other parties), each party covenanting to be legally bound hereby, do agree as follows:

1. Creditors signatory hereto hereby make, constitute, and appoint the parties of the second part and their respective successors, as the Creditors' Committee under this agreement, with all of the rights and privileges vested in the aforesaid Committee hereunder.

2. That the books, records, and papers of the Debtor shall at all times be open to the inspection of the said Creditors' Committee and/or any of the Creditors of the Debtor.

3. That Committee shall have the right to accept or refuse all contracts that may be offered to Debtor hereafter, and shall have control of all goods and merchandise that may hereafter be purchased by Debtor and the salaries and [fol. 13] wages to be paid to any and all employees of Debtor and of such details of the business of Debtor as may be necessary in order that it may be conducted to the best advantage of Creditors.

4. Creditors signatory hereto hereby extend the time for Debtor to pay its present indebtedness to them for the period of six months from the effective date of this agreement, and further agree to vest in Committee the authority to postpone the payment of said indebtedness for the further period of six months thereafter if, in Committee's discretion, such further postponement of indebtedness is in the interest of Creditors.

5. Creditors agree that, while this agreement is in effect, no action shall be brought to enforce the collection of Creditors' claims now due; but nothing herein contained shall constitute a limitation upon the rights of creditors to en-

force their respective claims at the conclusion of this agreement.

6. Debtor will, during the term of this agreement, act under the advice of Committee and will, at the end of each week, make and deliver to Committee a general account of its receipts and disbursements and of other matters or transactions relating to the general conduct of its business up to the end of the week next preceding, as shall be requested by Committee. Committee may, at any reasonable time, examine the books of Debtor and investigate its receipts and disbursements and the general conduct of its business, and for this purpose shall have the right to employ a certified public accountant at the expense of Debtor.

7. Committee shall have the right to make provision for and to deal with any claim, lien, or obligation which may affect the assets of Debtor, and may liquidate, settle, compromise, and adjust any such claim or claims upon such terms as in its judgment may be for the best interest of all parties hereto.

8. Committee shall serve without compensation, and shall not be responsible, either as individuals or collectively, for [fol. 14] any matter or thing hereunder, except that each member of Committee shall be responsible only for his own willful misconduct. Any member of Committee and any firm or corporation in which any such member is interested, may sell merchandise and loan money to Debtor and become pecuniarily interested in any transaction to which Debtor may be a party, or in which it may have an interest, or be in any way concerned.

9. Creditors hereby agree that their claims, as of April 27th, 1938, are hereby subordinated in payment to all new liabilities assumed by Debtor, including money borrowed and merchandise purchased in the ordinary course of business subsequent to April 27th, 1938, and to the costs and expenses of the Creditors' Committee, its agents, attorneys, and representatives.

10. Any vacancy in Committee arising from any cause whatsoever shall be filled by the vote of the surviving or remaining members of Committee. Any member of Committee shall have the right at any time to resign or withdraw. In all action to be taken by Committee, a majority

shall control. Any member of Committee may vote by proxy at any meeting of Committee.

11. Debtor will pay the reasonable expenses and disbursements of Committee incurred in the performance of their rights and duties under this agreement.

12. Debtor agrees to continue the Corn Exchange National Bank and Trust Company of Philadelphia as its banking depository, and no change in its banking depository shall be made without the consent of the Committee. All moneys received by Debtor and all disbursements of Debtor shall be made from said bank account, and all checks, drafts, bills of exchange, and other negotiable instruments shall be signed by an officer of Debtor and L. Norris Hall, chairman of said Committee.

13. No dividends on the stock of Debtor shall be declared or paid during the term of this agreement.

fols. 15-19/ 14. It is the intent of this agreement that the business of Debtor shall be continued during and for such time as Committee shall deem it to the best interest of Creditors to have it continued, and such business shall be discontinued, liquidated, and wound up at any time that Committee may so direct; and Debtor expressly covenants that it will make such necessary transfers of its assets and execute such instruments as may be necessary to carry out the wishes of Committee, if Committee shall determine at any time that discontinuance, liquidation, and winding up of Debtor and/or its business shall be advisable.

15. This agreement shall be deemed to be made under and governed by the laws of the State of Pennsylvania, including all matters of construction, validity and performance.

16. This agreement shall be considered executed on the 27th day of April, 1938, although signed by the parties hereto from time to time thereafter on this or on duplicate original copies hereof, all of which shall be considered as one instrument, with the same force and effect as if the signatures thereto were upon one paper and executed at one and the same time. It shall be binding upon the parties hereto, their and each of their respective executors, administrators, successors, and assigns.

Witness the signatures and seals of the parties hereto as of the day and year first above written.

Quaker City Sheet Metal Co., by E. C. Dearden, Jr., President.

Attest: Robert M. Carrigan, Secretary.

[Five duplicate originals each signed by one of the following:]

Wm. A. Simpson & Son, B. M. Simpson, Secy. (Seal.)

Apollo Steel Co., by A. M. Oppenheimer, Pres. (Seal.)

Chase Brass & Copper Co. Incorporated, V. W. Heyden, Asst. Treas. (Seal.)

L. Norris Hall, Inc., L. Norris Hall, Pres. & Treas. (Seal.)

Wheeling Corrugating Co., E. A. Rose, Treas. (Seal.)

[fol. 20] In United States District Court.

[Title omitted]

Trustee's Answer to Reclamation Petition of Edward C. Dearden, Sr.

United States of America,
Eastern District of Penna., ss:

Norman Klauder, being duly sworn according to law, deposes and says that he is the Trustee for the Estate of the above named Bankrupt and upon information and belief, makes answer to the allegations contained in the Reclamation Petition of Edward C. Dearden, Sr., as follows, to wit:

1. Admitted.

2. Admitted.

3. Deponent is informed, believes and avers that there is no averment of fact in the Third Paragraph of the Reclamation Petition requiring answer and hence makes none.

4. Deponent admits that the Bankrupt was engaged in the business of fabrication, erection and sale of all types

of sheet metal work; that during the Spring of 1938 it became financially involved and that at the instance of its larger creditors a Creditors' Committee was formed to represent creditors joining in a creditors' agreement and to supervise the business of the company in the interests [fol. 21] of the creditors and that the Committee, consisting of L. Norris Hall, V. W. Hayden, B. M. Simpson and Norman Klauder was formed under the terms of an agreement dated April 27th, 1938, all of which is set forth at length and at large in Exhibit "B" attached to the Reclamation Petition and that substantially all of the then important creditors of the company executed the agreement and that those so signing appointed the Committee as their agent in connection with the affairs of the company. Deponent admits that the agreement was signed by or on behalf of Apollo Steel Company, Chase Brass & Copper Co., L. Norris Hall, Inc., Wheeling Corrugating Co. and William A. Simpson & Son, but denies that the claims of those creditors aggregate approximately 80% of the present unsecured claims of creditors of the Bankrupt, all of which will more fully appear by a reference to the schedules of the Bankrupt, as well as in the proofs of claim filed in this proceeding.

5. Admitted.

6. Deponent admits that the Creditors' Committee, functioning as a representative of the creditors signatory, supervised and was familiar with the activities of the company from the time of its inception until the date of bankruptcy and admits that shortly prior to April 12th, 1940 the company, having exhausted its cash and being unable to meet its current expenses, was faced with the necessity of raising funds for its payroll as well as other operating expenses. Deponent, upon information and belief however, denies that the Creditors' Committee urged the President of the company to secure the loan of $1550.00 from the Reclamation Petitioner or that it was suggested through the attorneys for Creditors' Committee, Jenkins, Bennett and Libby, Esquires, that the loan be obtained and secured by [fol. 22] an assignment of a certain contract between the company and the York Ice Machinery Corporation as averred in the Sixth Paragraph of the Reclamation Petition. If it be material, deponent admits, however, that the loan of $1550.00 was obtained from the Reclamation

Petitioner on or about April 12th, 1940 and was secured or intended to be secured in the fashion more particularly described in the agreement bearing the same date thereof, attached to and made a part of the Reclamation Petition and marked Exhibit "A".

7. Admitted.

8. Admitted.

9. Admitted

10. Admitted.

11. Admitted.

12. Admitted.

13. Facts as averred admitted and materiality denied.

Deponent is informed, believes and therefore avers that no notice of the Assignment of the account, contract and or order was ever given by Edward C. Dearden, Sr., the Reclamation Petitioner, to the York Ice Machinery Corporation; that after the date of the said Assignment unrestricted dominion over the said contract, account and or order was exercised by the Quaker City Sheet Metal Company up until the date of bankruptcy, as a consequence of which deponent is informed by counsel, believes and therefore avers that the surrender and or delivery of the sum of $1550.00 or any other sum or part thereof to Edward C. Dearden, Sr., the Reclamation Petitioner, would constitute [fol. 23] a preferential payment within the meaning of the Bankruptcy Act of 1898 as amended and that consequently the prayer of the Petition should be denied.

Wherefore, deponent prays that the Petition be dismissed with costs.

Norman Klander.

Sworn to and subscribed before me this 7th day of March, A. D. 1941. Chas. H. Ward, Notary Public. My Commission Expires March 5, 1948.

[fols. 24-25] IN THE DISTRICT COURT OF THE UNITED STATES

[Title omitted]

Statement of Evidence

Hearing before Henry W. Braude, Esq., Referee, sur claims of Edward C. Dearden, Sr., held at the offices of the said Referee, room 3038, United States Court House, Philadelphia, Pa., on Thursday, March 27, 1941, at 3:00 o'clock P. M., pursuant to notice.

Present: Henry W. Braude, Esq., Referee. Bertram Bennett, Esq., for the Trustee. Lewis H. Van Dusen, Esq., for the Corn Exchange National Bank and Trust Company. William E. Mikell, Esq., for Edward C. Dearden, Sr.

CLAIM OF EDWARD C. DEARDEN, SR.

Mr. Mikell:

* * * * * * *

[fol. 26] I think that practically all of the pertinent facts are set forth and admitted in the petition of Edward C. Dearden, Sr. and the answer filed on behalf of Mr. Klauder as receiver and trustee.

I, therefore, assume that it can be agreed that the allegations of the petition of Edward C. Dearden, Sr., and the responsive answers of the receiver and trustee may be taken as having been read and offered in evidence, with the exception of the last paragraph of the answer which I do not [fol. 27] offer in evidence as it is not responsive to the allegations in the petitions, the conclusion of law,—I do not offer that in evidence.

The Referee: He undertook to decide the question:

Mr. Mikell: And I do not admit that no notice was given on behalf of Mr. Dearden to the York Ice Machinery Company prior to the bankruptcy in this matter. It is my contention that that is unnecessary.

* * * * * * *

[fols. 28-29] Mr. Bennett: There is no doubt that the Creditors' Committee knew these moneys were borrowed from Mr. Dearden, Sr., and that assignment was given to him as security.

If Mr. Mikell will make an offer of proof maybe we can agree to it.

Mr. Mikell: I offer to prove by Mr. Dearden that this particular loan, to be secured by the assignment in question, the papers for which were prepared on behalf of the Creditors' Committee by Mr. Bennett's firm, was the subject of a full meeting of the Creditors' Committee prior to the time it was assigned and authorized by them.

Mr. Bennett: That is right. I will agree to that.

* * * * * * * *

[fols. 30-35] In District Court of the United States for the Eastern District of Pennsylvania

In Bankruptcy

Cause No. 21312

In the Matter of Quaker City Sheet Metal Co., Bankrupt

Opinion and Order of Referee Sur Claim of Edward C. Dearden, Sr.

The amount involved in this reclamation petition is $1,550 and the factual situation is analogous to that of the Corn Exchange National Bank and Trust Co. claim, which was allowed as secured. (See opinion and order filed April 21, 1941). Here there was an assignment of a contract contemporaneously and in consideration of the loan. No notice was given to the debtor by the assignee prior to bankruptcy. The claim is allowed as a secured one.

Order

And Now, to wit, April 21, 1941, It Is Ordered, Adjudged and Decreed that the claim of Edward C. Dearden, Sr. must be, and hereby is, allowed as a secured claim in the sum of $1,550.

(S.) Henry W. Braude, Referee in Bankruptcy.

[fol. 36] IN UNITED STATES DISTRICT COURT

[Title omitted]

PROOF OF CLAIM.

Hector A. Sinzheimer, in the County of Montgomery, State of Pennsylvania, being duly sworn according to law, deposes and says:

1. That he is Assistant Vice-President of Corn Exchange National Bank and Trust Company, Philadelphia, a corporation organized and existing under the laws of the United States of America and carrying on business at 2nd and Chestnut Streets in Philadelphia, County of Philadelphia, State of Pennsylvania, and is duly authorized to make this proof of claim on its behalf.

2. That Quaker City Sheet Metal Company, a corporation, the above named Bankrupt, was at and before the filing against it of a petition for adjudication in bankruptcy, and still is, justly and truly indebted to said corporation in the sum of $7,954.51 with interest.

3. That the consideration for said debt is as follows:

(a) As to $119 thereof, moneys loaned and advanced to Quaker City Sheet Metal Company at its special instance and request, evidenced by the collateral promissory note (Exhibit 1) of Quaker City Sheet Metal Company dated January 19, 1940, in the amount of $1,930, payable on [fol. 37] demand. Claimant admits credits in the amount of $1,811 received on account of said note.

(b) As to $1,000 thereof, moneys loaned and advanced to Quaker City Sheet Metal Company at its special instance and request, evidenced by the collateral promissory note (Exhibit 2) of Quaker City Sheet Metal Company dated March 15, 1940, in the amount of $1,000, payable on demand.

(c) As to $2,200 thereof, moneys loaned and advanced to Quaker City Sheet Metal Company at its special instance and request, evidenced by the collateral promissory note (Exhibit 3) of Quaker City Sheet Metal Company dated March 23, 1940, in the amount of $4,280, payable on demand. Claimant admits credits in the amount of $2,080 received on account of said note.

(d) As to $540 thereof, moneys loaned and advanced to Quaker City Sheet Metal Company at its special instance and request, evidenced by the collateral promissory note (Exhibit 4) of Quaker City Sheet Metal Company dated March 29, 1940, in the amount of $540, payable on demand.

(e) As to $460 thereof, moneys loaned and advanced to Quaker City Sheet Metal Company at its special instance and request, evidenced by the collateral promissory note (Exhibit 5) of Quaker City Sheet Metal Company dated April 5, 1940, in the amount of $460, payable on demand.

(f) As to $1,450 thereof, moneys loaned and advanced to Quaker City Sheet Metal Company at its special instance and request, evidenced by the promissory note (Exhibit 6) of Quaker City Sheet Metal Company dated March 23, 1940, and payable May 31, 1940, in the amount of $1,450, and duly endorsed by Edward C. Dearden, Jr. and Robert M. Carrigan.

(g) As to $1,200 thereof, moneys loaned and advanced to Quaker City Sheet Metal Company at its special instance [fol. 38] and request, evidenced by the promissory note (Exhibit 7) of Quaker City Sheet Metal Company dated March 29, 1940, payable May 31, 1940, in the amount of $1,200, and duly endorsed by Edward C. Dearden, Jr. and Robert M. Carrigan.

(h) As to $1,000 thereof, moneys loaned and advanced to Quaker City Sheet Metal Company at its special instance and request, evidenced by the promissory note (Exhibit 8) of Quaker City Sheet Metal Company dated April 5, 1940, payable May 31, 1940, in the amount of $1,000, and duly endorsed by Edward C. Dearden, Jr. and Robert M. Carrigan.

(i) As to $4.36 thereof, interest upon Bankrupt's promissory note (Exhibit 1) in the amount of $1,930, dated January 19, 1940, upon the unpaid balances from April 1, 1940, to April 18, 1940, the date of the filing of the petition in bankruptcy.

(j) As to $3.00 thereof, interest upon Bankrupt's promissory note (Exhibit 2) in the amount of $1,000, dated March 15, 1940, upon the unpaid balances from April 1, 1940, to April 18, 1940, the date of the filing of the petition in bankruptcy.

(k) As to $10.41 thereof, interest upon Bankrupt's promissory note (Exhibit 3) in the amount of $4,280, dated March 23, 1940, upon the unpaid balances from April 1, 1940, to April 18, 1940, the date of the filing of the petition in bankruptcy.

(m) As to $1.07 thereof, interest upon Bankrupt's promissory note (Exhibit 5) in the amount of $460, dated 29, 1940, upon the unpaid balances from April 1, 1940, to April 18, 1940, the date of the filing of the petition in bankruptcy.

(n) As to $1.07 thereof, interest upon Bankrupt's promissory note (Exhibit 5) in the amount of $460, dated [fol. 39] April 5, 1940, upon the unpaid balances from April 5, 1940, to April 18, 1940, the date of the filing of the petition in bankruptcy.

The aggregate of the foregoing amounts is $7,989.46. Of this amount, $6,476.31 was advanced expressly to meet the bankrupt's payroll, and all of this money was in fact used to pay wages earned within three months of the filing of the petition in bankruptcy, which would otherwise have constituted claims against this estate entitled to priority, no one of which claims would have equalled $600 for any one wage claimant. These advances to meet payroll are evidenced by the aforementioned exhibits, and are entitled to prior payment as claims entitled to priority by way of subrogation to and assignment of the wage claims which they in fact were used to pay. The balance of $1,478.20 is a secured claim without priority.

Claimant acknowledges credit against said indebtedness in the amount of $34.95, being the balance standing to the credit of said bankrupt with claimant upon the date of the filing of the petition in bankruptcy, making the net amount of claimant's partially secured claim not entitled to priority $1,478.20, and of its partially secured claim entitled to priority $6,476.31.

4. No part of said debt has been paid except as stated.

5. There are no set-offs or counter-claims against said debt.

6. That said corporation, claimant herein, does not hold, and has not, nor has any person by its order, or to this deponent's knowledge or belief, for its use, had or received

any security or securities for said debt, except the following accounts receivable which were assigned as collateral security for the payment of said notes in accordance with the terms of Exhibits, 1, 2, 3, 4 and 5 and other instruments of assignment:

Riggs Distler & Co., Inc.,	in the face amount of	$524.37
Pennsylvania Engineering Co.,	" " " "	1,407.88
C. C. Kottcamp & Son	" " " "	2,751.33
" " " "	" " " "	108.00
" " " "	" " " "	112.47
Achenbach & Butler, Inc.,	" " " "	426.95
Peters Engineering Co.,	" " " "	173.63
" " "	" " " "	75.82
Alfol Insulation Co., Inc.,	" " " "	137.49
Ehret Magnesia Mfg. Co.,	" " " "	228.06
		$3,946.00

[fol. 40] *And except further* an assignment of the moneys due under a certain contract dated June 29, 1939, between Quaker City Sheet Metal Company and William H. Walters & Sons, under which the said Bankrupt agreed to supply sheet metal, and to do sheet metal work at the Eastern Regional Agricultural Research Laboratories in Wyndmoor, Pennsylvania, in accordance with an agreement of assignment, copy of which is attached hereto and made a part hereof, and marked Exhibit 9. Claimant advanced moneys to the Bankrupt, on the dates shown, to meet the payroll of the said Bankrupt under the said contract with William H. Walters & Sons. The amount of said fund to which the claimant is entitled under said assignment is not presently exactly ascertainable. *And except further* an assignment of the moneys due under a certain contract dated May 24, 1939, between Quaker City Sheet Metal Company and C. C. Kottcamp & Son, under which materials were to be supplied and work done by Bankrupt upon the Municipal Court Building, 19th & Vine Streets, Phila., Pa., in accordance with an agreement of assignment, copy of which is attached hereto and made a part hereof, marked Exhibit 10. The amount of said fund to which the claimant is entitled under said assignment is not presently exactly ascertainable.

7. That the true and correct copies of the aforesaid notes, with all indorsements, are attached hereto and made a part hereof, marked Exhibits 1, 2, 3, 4, 5, 6, 7 and 8, respectively.

* * * * * * *

[fol. 41] In Witness Whereof said Corn Exchange National Bank and Trust Company, Philadelphia, has caused these presents to be executed by its proper officer, and its corporate seal, duly attested, to be hereunto affixed, the 9th day of May, 1940.

Hector A. Sinzheimer, Assistant Vice-President of said Corporation. (Seal.)

Corn Exchange National Bank and Trust Company, Philadelphia, by Hector A. Sinzheimer. (Corp. Seal.)

Signed, Sealed and Delivered in the Presence of: W. J. Smedley.

Attest: B. G. Walton, Asst. Cashier.

Duly sworn to by Hector A. Sinzheimer. Jurat omitted in printing.

[fols. 42-43] EXHIBIT #1

$1,930.00. Philadelphia, January 19, 1940.

On Demand after date without defalcation for value Received We promise to pay to the order of Corn Exchange National Bank and Trust Company, Philadelphia Nineteen Hundred Thirty Dollars With Interest, having deposited as collateral security for payment of this or any other liability or liabilities to the holder hereof, due or to become due, or that may be hereafter contracted, the following property, viz.:

Assigned accounts receivable in sum of $2,416.76.

Quaker City Sheet Metal Co., E. C. Dearden, Jr., Pres. L. Norris Hall.

Payable at Corn Exchange National Bank and Trust Company, Philadelphia.

EXHIBITS 2, 3, 4, AND 5, except for amounts and dates, are substantially identical to Exhibit 1.

(Here follows 1 photolithograph, side folio 44)

EXHIBIT #6

COPY COPY COPY

$ 1,450.00 PHILADELPHIA March 23, 1940

ON May 31 1940 AFTER DATE We PROMISE TO PAY TO

THE ORDER OF Corn Exchange National Bank [illegible] Company

AT CORN EXCHANGE NATIONAL BANK
AND [illegible] COMPANY
[illegible]ELPHIA.

Fourteen Hundred Fifty 00/100 DOLLARS

WITHOUT DEFALCATION VALUE RECEIVED.

Quaker City Sheet Metal Co.
E. C. Dearden, Jr.
L. Norris Hall

No. DUE

[fol. 45] Exhibits 7 and 8, except for dates and amounts, are substantially identical to Exhibit 6.

[fol. 46] Exhibit #9

Copy

Assignment of Order

Know All Men by these Presents, that the Quaker City Sheet Metal Co., hereinafter called "Company," in consideration of the sum of One Dollar and other good and valuable considerations, the receipt of which is hereby acknowledged, has bargained, sold, assigned, transferred and set over, and by these presents does bargain, sell, assign, transfer and set over unto Corn Exchange National Bank and Trust Company, Philadelphia, its successors and assigns, hereinafter, sometimes called "Bank," all moneys now due and payable and/or which may hereafter become due and payable to Company from William H. Walters and Sons of 1310 N. Carlisle Street, Philadelphia, hereinafter called "Purchaser," under an existing contract between Company and Purchaser resulting from an order dated June 29, 1939, for sheet metal work at the Eastern Regional Agricultural Research Laboratory in Wyndmoor, Penna., given by Purchaser to Company, which order was accepted by Company on —— —, ——, and all Company's right, title, interest, claim and demand in and to all said moneys and every part thereof.

To Have and to Hold, to the said Corn Exchange National Bank and Trust Company, Philadelphia, its successors and assigns, from henceforth to its and their own proper use and benefit forever.

Company hereby constitutes and appoints the President or any Vice-President, for the time being, of Bank its true and lawful attorney irrevocable with full power of substitution, hereby giving and granting to him, them, or any of them, or any substitute, full power and authority in the name of Company, its successors, and assigns, but to the only proper use of Bank, its successors and assigns, to ask, demand, sue for, recover, receive, compound, acquit, release and discharge said moneys, or any part thereof, and upon receipt of the same or any part thereof, acquittances,

or other proper discharges to make and deliver, and generally for it and in its name, or in the names of its successors and assigns, to make, do, perform and execute all and every such further and other acts, matters and things touching and concerning the premises as to the said attorney, or any substitute, shall deem requisite, and that as fully and effectually to all intents and purposes as it, its successors and assigns, could or might have done, hereby ratifying and confirming all and whatever said attorney, or any substitute shall lawfully do or cause to be done in or about the premises.

Company hereby covenants and agrees to and with Bank, its successors and assigns, that it has not done or suffered, and that it or its successors and assigns, shall not or will not do or suffer any act, matter or thing whereby or by reason whereof Bank, its successors and assigns, shall or may be hindered or prevented from recovering or receiving the said moneys or any part thereof hereby assigned, or such other satisfaction as can or may be had or obtained for the same by virtue of this agreement or otherwise howsoever.

Company further covenants that it, its successors and assigns shall and will at all times hereafter, at the request of Bank, its successors and assigns, make, do and execute all such further and other acts and deeds as shall be reasonably required for the proving of the debt arising out of said contract, and the better and more effectually enabling them to recover, receive and enjoy the same according to the true intent and meaning of these presents; and especially that, after the merchandise specified or described in said contract has been shipped to Purchaser, Company will make proper notations upon its books, and/or records showing the assignment to Bank of the moneys due to Company by Purchaser, and will execute and deliver to Bank a further assignment, in form satisfactory to Bank, of the claim or account arising out of the delivery of said merchandise to, and the acceptance thereof by, Purchaser.

Company agrees that all checks, notes, drafts, moneys or other mediums of payment of any kind, which are received on account of or in payment of any moneys due under said contract, as well as any goods or merchandise delivered thereunder, which are returned to Company, shall be the sole property of Bank, and shall be immediately paid, trans-

ferred, turned over, and delivered to Bank by Company, and until so paid, transferred, turned over and delivered, it is hereby expressly agreed that all checks, notes, drafts, moneys or other mediums of payment and property so received shall be held by Company as trustee under this agreement for Bank.

Company hereby expressly authorizes Bank by its officers and agents to endorse Company's name upon and negotiate for the use of Bank all commercial paper payable to Company's order representing moneys due under said contract which may come into Bank's hands.

The within assignment shall constitute full and complete authority in and to Purchaser, his or its heirs, executors, administrators, successors and/or assigns, to make payment to Bank, its successors and assigns, of all sums due or to become due under said contract, and shall further constitute a request and direction by Company to Purchaser to make such payments to Bank, its successors and assigns, and upon such payments being made by Purchaser, the same shall constitute a full and complete payment and discharge of liability to Company to the extent of such payments respectively.

The within assignment is made and executed by Company in accordance with the authority given to the undersigned officers by the Board of Directors thereof.

Witness the common or corporate seal of Quaker City Sheet Metal Co. hereunto affixed, duly attested, this 20th day of October, A. D. 1939.

By E. C. Dearden, Pres. Attest: L. Norris Hall, Chairman of Creditors Committee.

The undersigned hereby acknowledges receipt of an executed original of the foregoing assignment, dated Philadelphia, —— —, 193—.

[fols. 47-50] Except for the name of the Purchaser, the nature of the work, and dates, Exhibit 10 is identical to Exhibit 9.

[fols. 51-54] In United States District Court

[Title omitted]

Statement of Evidence

Hearing before Henry W. Braude, Esq., Referee, sur claims of the Corn Exchange National Bank and Trust Company, held at the offices of the said Referee, room 3038, United States Court House, Philadelphia, Pa., on Thursday, March 27, 1941, at 3:00 o'clock P. M., pursuant to notice.

Present: Henry W. Braude, Esq., Referee. Bertram Bennett, Esq., for the Trustee. Lewis H. Van Dusen, Esq., for the Corn Exchange National Bank and Trust Company. William E. Mikell, Esq., for Edward C. Dearden, Sr. Edward C. Dearden, Sr., a witness. Hector A. Sinzheimer, a witness.

Colloquy between Referee and Counsel

. . . . . .

[fol. 55] Mr. Bennett: I think that we can boil it down considerable by agreement.

The trustee is willing to concede that the claim of the Corn Exchange National Bank and Trust Company amounting to $7954.51, as shown in its proof of claim and is composed as therein shown, in that on the dates shown certain moneys were advanced to the bankrupt, more particularly——

[fols. 56-57] The Referee: That no portion of the claim is secured?

Mr. Bennett: We say that no portion is secured; the loans and the dates——

The Referee: Are they correctly set forth in the proof?

Mr. Bennett: Yes, sir. If the proof of claim can be incorporated in the record, I have no objection.——

Mr. Van Dusen: You admit the facts appearing in the proof of claim are correct, but you say that due to the fact that no notice was given to the debtor of the assignment prior to the bankruptcy, the assignment, although made——

Mr. Bennett: Are ineffective as against the trustee.

. . . . . .

[fols. 58-59] Mr. Van Dusen: I would like to make the stipulation on the record, to see if Mr. Bennett agrees to it;

That paragraphs four, five, six, and seven of Mr. Mikell's petition on behalf of Edward C. Dearden, insofar as they are admitted by the trustee's answer, that those items to be treated as part of our case, and that it can be so stipulated?

Mr. Bennett: I believe that the entire answer, insofar as it is responsive to the petition and constitutes an admission to any allegation in the petition of Mr. Dearden, shall be applicable either to Mr. Dearden or to the Corn Exchange National — and Trust Company.

Mr. Van Dusen: That is satisfactory.

. . . . . .

[fol. 60] Mr. Van Dusen: May I ask Mr. Bennett this: Mr. Bennett, do you agree that these assignments which are in contest in our case were all made with the knowledge and the approval of the creditors Committee?

Mr. Bennett: Of the Creditors Committee, certainly.

. . . . . .

[fol. 61] Mr. Bennett: I will not go that far. I am not [fol. 62] asking that as a part of my agreement, but if that is important we can cover that later. The only thing that I am asking you to agree to is that you did not give any of the debtors notice of the assignment prior to bankruptcy?

Mr. Van Dusen: That is agreed to.

. . . . . .

Mr. Bennett: On that score, subject to what Mr. Dearden will say, are you willing to agree to that portion, that no [fol. 63] notice was given to any of the accounts.

Mr. Van Dusen: I agree that no notice was given by the bankrupt prior to the bankruptcy.

. . . . . .

[fol. 64] EDWARD C. DEARDEN, JR., having been duly sworn, was examined and testified as follows:

Direct examination.

By the Referee:

Q. Your full name?
A. Edward C. Dearden, Jr.

. . . . . .

[fol. 65] By Mr. Van Dusen:

Q. You were president of the Quaker Sheet Metal Company?
A. I was.
Q. When did you become president?
A. Sometime in 1936.
Q. And the company got into financial difficulties in the spring of 1938?
A. That is correct.
Q. What was the situation at that time?
A. Insufficient working capital to permit the company to carry out contracts then existing on its books.
Q. Then what did you do?
A. We called together the five principal creditors of our company and explained to them that we had these contracts to do or to complete, and that we did not have sufficient working capital to do it, and asked them to enter into some kind of an agreement to subordinate their claims and enable us to continue in business.

. . . . . .

[fol. 66] Q. And approximately what percentage of your total indebtedness was owing to these creditors?
A. At that time it was between 75 and 80 per cent.

Mr. Bennett: At that time?
Mr. Van Dusen: Yes, at that time.

. . . . . .

Q. Now, was there an agreement drawn up?
A. There was.

Mr. Bennett: Show it to him.

By Mr. Van Dusen:

Q. I show you a document here (producing same). Is [fol. 67] that the agreement that was executed by the creditors that I mentioned?

A. It is.

Q. And the Quaker City Sheet Metal Company?

A. It is.

Q. Did you have any discussion with the representative of the Corn Exchange at that time?

A. Yes.

Q. And what was the arrangement you made with that bank?

A. The arrangement,—let me put it this way,—it was rather mutual or allied,—the Creditors Committee, the five creditors, were anxious to execute an agreement so that we could continue in business, and we were naturally interested in finding out if the Corn Exchange Bank would finance the company as it had before. My partner and myself made several calls on the Corn Exchange Bank.

Q. This is at the time of the execution of the agreement?

A. After the first meeting but before the final execution of the agreement.

The Corn Exchange bank agreed to loan us money upon collateral, and upon reporting that back to the five cred- [fol. 68] itors they agreed to sign the agreement, and copies of the agreement were sent to the various home offices of the creditors for signature. Before they were returned completed signed, Mr. Carrigan, my partner and myself——

Q. By partner, you mean the other officer of the company?

A. The other officer of the company, myself, and Mr. Hall, went down, and had a discussion with the bank along the same general lines that Mr. Carrigan and I had been discussing with them before.

Q. Mr. L. Norris Hall, chairman of the Creditors' Committee?

A. That is right, yes, sir.

Q. He was president of L. Norris Hall, Inc.?

A. Yes, sir.

Q. And which is one of the creditors that signed the agreement?

A. That is right.

Q. This arrangement that you made with the bank was part of the general scheme that had to be worked out before the agreement could be executed?

A. That is right.

Q. What were you going to give the bank as security for these advances to carry out the contract?

A. Accounts receivable.

[fol. 69] By Mr. Van Dusen:

Q. Will you explain to His Honor just how these loans were made by the Corn Exchange?

A. Well, we were in the contracting business, and at the end of every month we sent to our customers requests for payment, as is usual in the contracting business, for the value of the work we had performed during that month. As we needed the money we would take these accounts receivable down to the Corn Exchange Bank and pledge them as collateral for a loan.

Q. Did you make any notations on your books of these assignments?

A. Yes, and on the copies of the invoices.

Q. Where did that appear on the books?

A. They were on the top of the ledger sheets.

Q. Stamped?

A. Stamped on the top of the ledger sheets.

Q. What was stamped there?

A. "For value received this account has been assigned to the Corn Exchange National Bank and Trust Company," [fol. 70]—I forget the exact wording of it,—but it was the wording that the Corn Exchange wanted us to put on them.

Q. When these accounts were collected, how were they collected?

A. The payment was received by the company and the check was taken down and given to the Bank.

Q. In other words, you took the checks in payment of the accounts to the Bank? You never deposited the checks in your own account?

A. Never.

Q. You took it to the Corn Exchange?

A. That is correct.

By the Referee:

Q. Did you conform to that practice throughout the entire time?

A. Throughout the entire time, yes.

Q. And this was in keeping with the arrangements with the Corn Exchange?

A. That is correct.

By Mr. Van Dusen:

Q. You subsequently entered into a new contract?

A. That is correct, a larger one.

Q. What was the procedure in connection with this contract?

[fol. 71] A. The procedure in that case, where we needed finances fast, was to assign the contract itself to the Bank.

Q. By that you mean the moneys due under the contract?

A. The moneys due under the contract itself, to the Bank.

Q. The Bank did not assume any obligations under these contracts?

A. None whatever.

Q. Well, now, when you decided to take these new contracts, or before you decided to take new contracts, did you discuss the matter with the Creditors' Committee and the Corn Exchange?

A. First, with the Creditors' Committee, and then after their approval, with the Corn Exchange, and find out if it was a job too much for us to finance,—whether it could be financed in our regular routine of business, and when I had received the approval from both parties we accepted the contract.

Q. Who was on the Committee,—L. Norris Hall, representing L. Norris Hall, Inc., V. W. Heyden, representing the Chase Brass & Copper Co., W. W. Keefer, representing the Apollo Steel Co., B. M. Simpson, of W. A. Simpson & Son, and Norman Klauder, representing the Wheeling [fol. 72] Corrugating Company?

A. That is correct.

Q. And they met about once a month?

A. I would say on an average of once a month.

Q. Mr. Hall was chairman?

A. That is correct.

Q. And he countersigned all checks?

A. Yes, sir.

Q. And he executed the assignments under the contract?
A. That is also correct.
Q. And he signed the notes, too?
A. Yes, he did.
Q. To the bank?
A. Yes.
Q. Mr. Hall and the Committee supervised the conduct of your business?
A. They did.
Q. Mr. Hall was there frequently?
A. Yes, very frequently.
Q. How frequently?
A. Well, twice a week, sometimes oftener.
Q. Were these moneys due under contract assigned at the time the contract was executed?
A. No. The actual assignments would be made some- [fol. 73] time shortly after the contract was accepted. We could not assign something we did not have.
Q. When the Corn Exchange put up some money?
A. No, prior to that.
Q. As the accounts receivable became due under the contract, then they were assigned?
A. That is correct. But, I think I should say here that the Corn Exchange advanced us money for payroll purposes on these contracts prior to the expiration of any one month; in other words, that enabled us to build up the accounts receivable which at the end of the month would then be assigned to the Corn Exchange Bank.
Q. All of the advances, though, were made subsequent to the assignments of moneys due under the contract?
A. Absolutely.
Q. And by the assignment of the money due under the contract you were obligated to assign the accounts receivable under such contract?
A. That is correct.

. . . . . .

[fol. 74] Mr. Bennett: They had double protection themselves—they not only had the assignment of the contract but they also took the assignment of the invoices.

. . . . . .

[fols. 75-76] By Mr. Van Dusen:

. . . . . .

[fols. 77-78] Q. And all of these pledges and assignments were made in consideration of advances by the Bank at the time?

A. That is right.

. . . . . .

[fol. 79] Recross-examination.

By Mr. Bennett:

. . . . . .

[fols. 80-81] Q. Were the invoices which were sent to the customers marked so as to indicate that they were payable by the customer to the Corn Exchange National Bank and Trust Company?

A. No.

Q. They were not. You are definitely certain that the copies of the invoices that were put in your folder contained such a notation?

A. Yes.

. . . . . .

[fol. 82] Hector A. Sinzheimer, having been duly sworn, was examined and testified as follows:

Direct examination.

By the Referee:

Q. What is your full name?

A. Hector A. Sinzheimer.

Q. And your address?

A. 1510 Chestnut Street.

. . . . . .

[fols. 83-92] Mr. Van Dusen: I would like to prove by Mr. Sinzheimer that, first of all, this agreement was extended from time to time by letters written by the creditors to him——

Mr. Bennett: There is no doubt of that, that the Creditors' Committee agreement was extended from time to time notwithstanding its date, until after bankruptcy, October 24, 1940.

Mr. Van Dusen: October 24, 1940.

Mr. Bennett: Yes, that is my understanding—it was in effect at the time of bankruptcy. Obviously, it could not be in effect thereafter, only in so far as it applied to the right of subrogation.

Mr. Van Duser: And secondly, I offer to prove by Mr. Sinzheimer that these loans made by the Corn Exchange from the time of the inception of the subordinate agreement were made with the knowledge and consent of Mr. Hall, representing the Creditors' Committee, and Mr. Sinzheimer of the Bank, and that the Bank advanced this money in consideration of these assignments—for present consideration—and that the moneys have not been paid as set forth in the proof of claim.

Mr. Bennett: I will agree to that.

. . . . . .

[fol. 93] In the District Court of the United States for the Eastern District of Pennsylvania.

In Bankruptcy

Cause No. 21312.

In the Matter of Quaker City Sheet Metal Co., Bankrupt

Opinion and Order of Referee Sur Claim of Corn Exchange National Bank and Trust Co.

This controversy between the trustee in bankruptcy and the assignee of accounts receivable, to whom the assignments were made by the bankrupt as security for loans, arises by reason of the language incorporated in the completely revamped Sec. 60 of the Chandler Act, dealing with preferences.

Sec. 60 (a) provides:

"(a) 'A preference is a transfer, as defined in this Act, of any of the property of a debtor to or for the benefit of a creditor for or on account of an antecedent debt, made or suffered by such debtor while insolvent and within four months before the filing by or against him of the petition in bankruptcy or of the original petition under Chapter X, XI, XII, or XIII of this Act, the effect of which transfer

will be to enable such creditor to obtain a greater percentage of his debt than some other creditor of the same class. For the purposes of subdivisions (a) and (b) of this section, a transfer shall be deemed to have been made at the time when it became so far perfected that no bona fide purchaser from the debtor and no creditor could thereafter have acquired any rights in the property so transferred superior to the rights of the transferee therein, and, if such transfer is not so perfected prior to the filing of the petition in bankruptcy or of the original petition under Chapter X, XI, XII or XIII of this Act, it shall be deemed to have been made immediately before bankruptcy."

Sec. 60 (b) provides:

"(b) Any such preference may be avoided by the trustee [fol. 94] if the creditor receiving it or to be benefited thereby or his agent acting with reference thereto has, at the time when the transfer is made, reasonable cause to believe that the trustee may recover the property, or, if it has been converted, its value from any person who has received or converted such property, except a bona fide purchaser from or lienor of the debtor's transferee for a present fair equivalent value; Provided, however, that where such purchaser or lienor has given less than such value, he shall nevertheless have a lien upon such property, but only to the extent of the consideration actually given by him. Where a preference by way of lien or security title is voidable, the court may on due notice order such lien or title to be preserved for the benefit of the estate, in which event such lien or title shall pass to the trustee. For the purpose of any recovery or avoidance under this section, where plenary proceedings are necessary, any state court which would have had jurisdiction if bankruptcy had not intervened and any court of bankruptcy shall have concurrent jurisdiction."

The facts of this case are not in dispute. In the spring of 1938, because the bankrupt found itself in financial difficulties for want of working capital, its principal creditors, whose claims now represent a large percentage of all the unsecured claims which have been proved against the bankrupt estate, agreed in writing—the agreement is dated April 27, 1938 and was extended from time to time until August 27, 1940, which is after the bankruptcy petition—to sub-

ordinate their claims to those who would advance the new working capital. Subsequent to the agreement, the creditors, through a creditors' committee, supervised the bankrupt's business and in May, 1938, arranged with the claimant bank for loans upon the security of bankrupt's accounts receivable, which arrangement was continued until the date of bankruptcy, the claimant advancing money and being repaid as the accounts were collected. The claimant was also given assignments of moneys due or to become due under certain contracts which the bankrupt was able to secure, in consideration of advances for payroll and other needs. [fol. 95] It cannot be denied that the creditors' committee knew that the accounts receivable and the assignments of the moneys due under the contracts were being given as collateral security for concurrent advances and that they gave their express approval thereto. It is also clear that the claimant gave no notice to the debtors prior to bankruptcy.

The question for determination is whether within the meaning of the language in the above-cited sections, in the absence of notice by the assignee to the debtors of the accounts receivable prior to bankruptcy, the trustee by operation of law became vested with title to the accounts.

The question has yet to be ruled in this jurisdiction, and the outcome of the dispute is being awaited with much concern by financial institutions, to whom the business of advancing money on the security of assigned accounts, without the necessity of giving notice to the debtors of the accounts, is accounted of the highest practical importance. It is also, of course, important to the small manufacturer or merchant, whose capital is limited and who must often have recourse to financing on the security of his receivables. But for the plainly declared and generally accepted substantive rule of law in Pennsylvania, requiring notice as between successive assignees, which must be observed in the disposition of this controversy—Erie v. Tompkins, 304 U. S. 64—so far as it may be affected by it, the decision of the Supreme Court in Sales Trust Co. v. Manufacturers Finance Co., 264 U. S. 182, and the ruling in other jurisdictions since the Chandler Act amendment could have been regarded as plainly answering the question in favor of the [fol. 96] assignee of the accounts. Re Johnson-Maas Co., Inc., 45 Am. B. R. (N. S.) 32, Advance Sheets, April 1941; Re Talbot Canning Corp., 35 Fed. Supp. 680; Adams v. City

Bank & Trust Co., 115 Fed. (2) 453; E. H. Webb Grocery Co., 32 Fed. Supp. 3.

But, as may readily be observed, Salem Trust Co. v. Manufacturers Finance Co. antedates Erie v. Tompkins and the other cases relied upon by the claimant were all determined on the basis of the substantive law of jurisdictions; which is concededly at variance with the Pennsylvania rule. The rule of law laid down in Phillips Estate (No. 3), 205 Pa. 515, following the English rule as exemplified in Dearle v. Hall, 3 Rus. 1-38, is that as between successive assignees of a fund in the hands of a third person, that assignee, without regard to the date of his assignment, who first gives the debtor notice of it is entitled to be paid first. The basis for the rule lies in the abhorrence of our common law for secret liens, and perhaps, also in the additional consideration that our limited equity jurisdiction requires that equitable principles be blended with common law principles to do adequate justice. As between two innocent parties to a transaction, the one who makes possible a fraud and a consequent injury to another is made to suffer the loss. The first assignee, by failing to give notice to the debtor, makes possible the commission of a fraud on the second bona fide assignee which by notice he could have prevented. Yet the meaning and purpose of the rule may not have the broad effect that, at first blush, it would seem to have in a situation, as here, where the contest is not between successive assignees but between the trustee in bankruptcy and an assignee, unless [fol. 97] it be determined that the trustee takes the place of a second bona fide assignee. If the latter premise is the correct one then it is clear the trustee must prevail. An examination into the rule, however, which has a bearing on the trustee's status, indicates that while the second assignee obtains a superior right to be paid by the debtor of the account, on the theory of an estoppel against the first assignee, the second assignee does not necessarily get a superior title to that of the first assignee. In other words, the second assignee merely gets a superior right to be paid by the debtor, because the debtor becomes a trustee for the assignee who first gives him notice. This is clearly indicated by Phillips Estate (No. 4), 205 Pa. 525, where an assignee who had given no notice of his assignment to the debtor was nevertheless held to have priority over a subsequent assignee who had given notice,

where an attachment had intervened against the fund between the dates of the assignments. The reason for this seeming contradiction of the general rule is, as the Court explains, that the claim under the attachment being prior to the last assignment because it took place before the last assignee gave notice to the debtor, the attaching creditor could take only what remained to the assignor. The attaching creditor could take only what the assignor could assign. "As to him the prior assignments, with or without notice to the accountants, were valid, and so they were as against his attaching creditors, whose rights rise no higher than his." (p. 531.)

The question then narrows itself down to the nature of the trustee's title to or interest in the accounts. Does he [fol. 98] stand in the shoes of a second assignee, that is, a bona fide purchaser, who is presumed to have given notice prior to bankruptcy, and thus has acquired a superior right to the proceeds of the accounts, or does he stand in the shoes of a creditor whose claim is either subject to the assignment or superior to it? Again, the State law must control the situation. State law controls as to what rights a lien or execution creditor could have. The validity of all liens, claims and equities is to be determined by the local law. Thompson v. Fairbanks, 196 U. S. 516; re Press Printers and Publishers, Inc., 24 F. (2) 34. The first supposition—that the trustee stands in the shoes of a bona fide purchaser—notwithstanding the possibilities that such a creditor assignee could well have existed must necessarily be excluded by the definition in the bankruptcy law of what constitutes the trustee's title. A second assignee could well have acquired superior right to payment of the accounts, if he had given notice prior to the bankruptcy. And if in theory, for purposes of bankruptcy administration, he is presumed to exist and the trustee succeeds to his rights then inevitably, it must be repeated, the trustee must prevail or arbitrarily there must be an election between the acceptance of this hypothesis and the conclusions to be drawn from the definition of the trustee's title. By Sec. 70 (a) the trustee is vested by operation of law with the title of the bankrupt as of the date of the filing of the petition in bankruptcy to (5) property, including rights of action, which prior to the filing of the petition he could by any means have transferred or which might have been levied upon and sold under judicial process against

him, or otherwise seized, impounded, or sequestered. This [fol. 99] definition in turn must be read in conjunction with the provision in Sec. 70 (c) which provides that "* * * the trustee, as to all property in the possession or under the control of the bankrupt at the date of bankruptcy or otherwise coming into the possession of the bankruptcy court, shall be deemed vested as of the date of bankruptcy with all rights, remedies and powers of a creditor then holding a lien thereon by legal or equitable proceedings, whether or not such a creditor actually exists; and, as to all other property, the trustee shall be deemed vested as of the date of bankruptcy with all the rights, remedies and powers of an attachment creditor then holding an execution duly returned unsatisfied; whether or not such a creditor actually exists."

Clearly, the bankrupt could not by any honest means have transferred the accounts after their prior assignment to the claimant; so that the trustee can take no title to the accounts, save subject to the prior assignment, on the score of that provision. The provision surely does not contemplate a dishonest transfer to enure for the benefit of creditors. Nor could there have been an attachment of the proceeds of the accounts and their sale under judicial process, save subject to the rights of the claimant assignee to priority in distribution, as declared by the Phillips case (supra); so that the trustee can acquire no superior right on that score. Is his status then modified by the provision which vests him, as to property in the bankrupt's possession or control or which otherwise comes into the possession of the bankruptcy court, "with all the rights, remedies, and powers of [fol. 100] a creditor then holding a lien thereon by legal or equitable proceedings?" Whatever lien the trustee could thus acquire on the proceeds of the accounts in the bankrupt's possession would necessarily be subject to the prior lien or title of the assignee. And as we have seen, if the trustee's claim is predicated as to outstanding accounts on "all the rights, remedies and powers of an attachment creditor then holding an execution duly returned unsatisfied", he takes subject to the assignment in any distribution which may thereafter follow. See Hawley Down-Draft v. Chidsey (3d Cir.) 238 Fed. 122—38 Am. B. R. 219.

If the foregoing reasoning is correct, then the trustee's contention, that by reason of the failure to give notice to the debtors, the assignment of the accounts to the claimant must be considered as having been made immediately be-

fore the bankruptcy, a fortiori it must be taken as a transfer for an antecedent debt and therefore voidable because the assignee had reasonable cause to believe the assignor was insolvent, must fail. The conclusion is that the assignments were made for a present consideration because the title to them became perfected when made.

This result obviates the need for consideration of the claimant's contention that in any event the creditors who were parties signatory to the subordination agreement are estopped from asserting their claims on a parity with it.

[fols. 101-105] ORDER

And Now, to wit, this 21st day of April, 1941, It Is Ordered, Adjudged and Decreed that the claim of the Corn Exchange National Bank and Trust Company be, and it hereby is, allowed as a secured claim in the sum of $7,954.51.

(Signed) Henry W. Braude, Referee in Bankruptcy.

[fol. 196] IN THE DISTRICT COURT OF THE UNITED STATES FOR THE EASTERN DISTRICT OF PENNSYLVANIA

No. 21312

In Bankruptcy

In re QUAKER CITY SHEET METAL CO., Bankrupt

ORDER AFFIRMING ORDERS OF REFEREE—Filed September 17, 1941

The orders of the Referee are affirmed.

By the Court, Kirkpatrick, J.

[fols. 107-112] In the District Court of the United States for the Eastern District of Pennsylvania

In Bankruptcy

Cause No. 21312

In the Matter of Quaker City Sheet Metal Co., Bankrupt

Final Decree—Filed November 10, 1941

Sur Certificate for Review

Re Claim of Corn Exchange National Bank and Trust Co.
Claim of Edward C. Dearden, Sr.

And now, to wit, November 10, 1941, this cause having come on to be heard and having been argued by counsel; and thereupon upon consideration thereof, it is

Ordered, Adjudged and Decreed that the Orders entered on April 21, 1941 by Henry W. Braude, Esq., Referee in Bankruptcy, as follows, to wit:

"And now, to wit, this 21st day of April, 1941, it is

Ordered, Adjudged and Decreed that the claim of the Corn Exchange National Bank and Trust Company be and it hereby is, allowed as a secured claim in the sum of $7,954.51."

"And now, to wit, this 21st day of April, 1941, it is Ordered, Adjudged and Decreed that the claim of Edward C. Dearden, Sr. must be and hereby is, allowed as a secured claim in the sum of $1,550.00."

Be and the Same Are Hereby Affirmed.

By the Court: (Sgd.) Kirkpatrick, J.

[fol. 113] Clerk's Certificate to foregoing transcript omitted in printing.

[fol. 114] Clerk's Certificate to foregoing transcript omitted in printing.

[fols. 115-116] **Proceedings in the United States Circuit Court of Appeals for the Third Circuit**

In United States District Court

Relevant Docket Entries

Omitted. Printed side page 1 ante.

[fols. 117-123] In United States District Court

Opinion and Order of Referee Sur Claim of Corn Exchange National Bank and Trust Company

Omitted. Printed side page 93 ante.

[fol. 124] Order

Omitted. Printed side page 101 ante.

In United States District Court

Opinion and Order of Referee

Sur Claim of Edward C. Dearborn, Sr.

Omitted. Printed side page 30 ante.

[fols. 125-138] In United States District Court

Memorandum

Sur Certificates for Review

Omitted. Printed side page 106 ante.

In United States District Court

Final Decree

Sur Certificate for Review

Omitted. Printed side page 107 ante.

[fol. 139] IN THE UNITED STATES CIRCUIT COURT OF APPEALS

[Title omitted]

MINUTE ENTRY OF ARGUMENT AND SUBMISSION

And afterwards, to wit, the 18th day of March, 1942, come the parties aforesaid by their counsel aforesaid, and this case being called for argument sur pleadings and briefs, before the Honorable Albert B. Maris, Honorable Charles Alvin Jones and Honorable Herbert F. Goodrich, Circuit Judges, and the Court not being fully advised in the premises, takes further time for the consideration thereof.

And afterwards, to wit, on the 12th day of August, 1942, come the parties aforesaid by their counsel aforesaid, and the Court, now being fully advised in the premises, renders the following decision:

[fol. 140] IN THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE THIRD CIRCUIT, OCTOBER TERM, 1941

No. 7893

In Re QUAKER CITY SHEET METAL CO., Bankrupt

Appeal of Norman Klauder, Trustee in Bankruptcy

Appeal from the District Court of the United States for the Eastern District of Pennsylvania

OPINION—Filed August 12, 1942

Before Maris, Jones and Goodrich, Circuit Judges

MARIS, *Circuit Judge:*

At the beginning of 1940 Quaker City Sheet Metal Company was in financial difficulties and unable to complete its contracts and meet its payroll for lack of working capital. Between January 19, 1940 and April 5, 1940 the Corn Exchange National Bank and Trust Company made several loans to the company. On April 12, 1940 Edward C. Dearden, Sr. made a loan to the company. Concurrently with each loan and as collateral security for it the company assigned contracts and the accounts receivable arising from

[fol. 141] the contracts. The assignments were made in Pennsylvania, with the knowledge and consent of a creditors' committee which represented most of the general claims against the company. Neither the bank nor Dearden gave notice of the assignments to the parties who owed the accounts receivable. On April 18, 1940 an involuntary petition in bankruptcy was filed against the company and on May 7, 1940 the company was adjudicated a bankrupt. At this time the company was indebted to the bank in the sum of $7,954.51 and to Dearden in the sum of $1,550. The bank filed a proof of claim as a secured creditor, to which the trustee in bankruptcy objected. An issue was framed upon a petition for reclamation filed by Dearden. Both claims were passed upon by the referee in bankruptcy who allowed them as secured claims. The District Court for the Eastern District of Pennsylvania entered a decree affirming the orders of the referee. The trustee in bankruptcy has taken this appeal. The trustee concedes the indebtedness but contends that the assignments are voidable preferences by virtue of subdivisions a and b of section 60 of the Bankruptcy Act, as amended, (11 U. S. C. A. § 96(a) (b)).

We are primarily concerned with the provisions of subdivision a of Section 60, which are as follows:

"a. A preference is a transfer, as defined in this Act, of any of the property of a debtor to or for the benefit of a creditor for or on account of an antecedent debt, made or suffered by such debtor while insolvent and within four months before the filing by or against him of the petition in bankruptcy, or of the original petition under chapter X, XI, XII, or XIII of this Act, the effect of which transfer will be to enable such creditor to obtain a greater percentage of his debt than some other creditor of the same class. For the purposes of subdivisions a and b of this section, a transfer shall be deemed to have been made at the time when it became so far perfected that no bona fide purchaser from the debtor and no creditor could thereafter have acquired any rights in the property so transferred superior to the rights of the transferee therein, and, if such transfer is not so perfected prior to the filing of [fol. 142] the petition in bankruptcy or of the original petition under chapter X, XI, XII, or XIII of this Act,

it shall be deemed to have been made immediately before bankruptcy."

It will be noted that the subdivision comprises two sentences. The first lays down the criteria for determining whether a transfer is preferential. The second sentence provides that for the purposes of subdivision a, inter alia, a transfer shall not be deemed to have been made until it has been perfected as against bona fide purchasers from and creditors of the debtor.

It will be seen that one of the criteria laid down by the first sentence of subdivision a for determining whether a transfer is to be treated as a preference is that it is "for or on account of an antecedent debt." The question with which we are primarily concerned in this case involves the meaning of this phrase. The question is this. In determining whether a debt is antecedent to a transfer made on account of it are we to apply the rule laid down in the second sentence as to when a transfer is to be deemed as having been made? In other words, is a debt to be treated as antecedent to a transfer actually made contemporaneously but not perfected as against purchasers and creditors of the debtor until a later time? We think that a fair construction of the statutory language requires an affirmative answer to this question. The rule which the second sentence of subdivision a lays down as to the time when a transfer is to be deemed to have been made is stated to be "for the purposes of subdivision a," inter alia. It is thus clear that the rule is intended to apply to the provisions of the first sentence of that subdivision insofar as they involved questions having to do with the time of making a transfer. There is no indication that its application to the first sentence is to be restricted to the mere determination of whether a transfer is made while the debtor is insolvent and within four months of bankruptcy. On the contrary it is obvious that the time of the making of a transfer is the essential element in de- [fol. 143] termining whether a debt on account of which it is made was antecedent to it.

We conclude that the rule laid down in the second sentence of subdivision a of Section 60 for determining the time of the making of a transfer applies to the determination of the question whether the transfer was made for or on account of an antecedent debt. In this conclusion we are

supported by students of the act who have forcefully pointed out that the purpose of Section 60a, as amended by the Chandler Act of 1938, was to strike down secret liens even though given for a present consideration.[1] We recognize that in the case of Adams v. City Bank and Trust Co., 115 F. 2d 453 (1940), the Circuit Court of Appeals for the Fifth Circuit reached a contrary conclusion but for the reasons which we have given we are unable to follow the construction of the statute made in that case.

There remains for consideration the question whether under the law of Pennsylvania subsequent bona fide assignees or attaching creditors of the company could have acquired rights to the accounts receivable here in question superior to the rights of the bank and Dearden under their prior assignments in view of the fact that the latter gave no notice of their assignments to the persons owing the accounts. In other words, since the bank and Dearden gave no such notice prior to bankruptcy, must the transfers to them be deemed under the provisions of Section 60a to have been made immediately before bankruptcy and, therefore, for antecedent debts? If so, it is clear that, since an assignment is a transfer within the definition of Section 1(30) of the Bankruptcy Act as amended (11 U. S. C. A. § 1(30)), their assignments were preferences which were voidable by the trustee under subdivision (b) of Section 60 if the other criteria laid down in Section 60 were present.

The trustee urges that under the law of Pennsylvania [fol. 144] a subsequent bona fide purchaser of the accounts receivable from the company could have acquired rights to the accounts superior to those of the bank and Dearden provided only that he gave notice before they did.[2] In

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[1] McLaughlin, Aspects of the Chandler Bill to Amend The Bankruptcy Act (1937), 4 U. of Chicago L. Rev. 369, 388; Mulder, Ambiguities in the Chandler Act (1940) 89 U. of Pa. L. Rev. 10, 25; 3 Collier on Bankruptcy (14th Ed.) § 60.48.

[2] The Pennsylvania Act of July 31, 1941, P. L. 606, § 1 (69 Pa. P. S. § 561), which dispenses with the necessity for the giving of notice of an assignment of accounts receivable if a record of the assignment is made upon the books of account of the assignor, can have no bearing upon the assignments in this case because they were made prior to the effective date of that act.

support of this proposition the case of Phillips's Estate (No. 3), 205 Pa. 515, 55 A. 213 (1903), is cited. That case involved a contest between successive assignees of a fund in the hands of a third person. The court found in favor of the subsequent assignee, adopting the rule that (p. 524) "if an assignee fails to give notice to the person holding the fund assigned to him, a subsequent assignee, without notice of the former assignment, will, upon giving notice of his assignment, acquire priority." It is argued by the bank and Dearden that the effect of this ruling is neutralized by another decision in the same estate handed down by the Pennsylvania Supreme Court on the same day, Phillips's Estate (No. 4), 205 Pa. 525, 55 A. 216 (1903), in which the court awarded priority to an assignee who had not given notice over a subsequent assignee who had given notice. It appeared that a claimant to a share in a decedent's estate had transferred his interest to successive assignees. The first did not give notice—the second did. In the period intervening between the two assignments a creditor of the claimant served the accountants with a writ of foreign attachment. The court awarded the creditor priority over the later assignee because his attachment was first in time. His lien, however, was subordinated to that of the first assignee. The court reasoned that as between the assignor and the assignee the assignment was valid whether with or without notice, that the creditor's right rose no higher and that he could attach only that which the assignor had left after the assignment.

It will be seen that the decision in Phillips's Estate (No. 4) involved the determination of the rights of an [Vol. 145] attaching creditor. The court's ruling was based upon the proposition that an attaching creditor could not secure rights superior to those of a prior assignee even though the latter had not given notice. The case, however, did not in any way modify the ruling in Phillips's Estate (No. 3) as to the position of a subsequent assignee who was first in giving notice. The rule as to the time of making a transfer, which is laid down in the second sentence of Section 60a, cannot operate to fix that time as of the time of actual transfer unless two bases for such operation are present. It must appear to have then been so far perfected that (1) no bonafide purchaser and (2) no creditor could thereafter have acquired superior rights in the property transferred. In the case before us it is immaterial that

Phillips's Estate, (No. 4), which deals with the rights of creditors, provides one of the bases for the operation of the rule in favor of the date of actual transfer since Phillips's Estate (No. 3), which fixes the rights of purchasers does not provide the other basis. As we have said, the statute requires the presence of both. Consequently if, as here, one is absent, the date of transfer must be deemed to be postponed to the later date fixed by the second sentence of subdivision a, in this case the date of bankruptcy. It follows that the assignments to the bank and Dearden must be deemed for the purposes of the administration of the company's estate in bankruptcy to have been made for or on account of antecedent debts of the company and must be treated as preferences voidable at the instance of the trustee in bankruptcy if the other elements of a voidable preference set forth in Section 60 are present."

The decree of the district court is reversed and the cause is remanded with directions to take such further proceedings therein as may be consistent with this opinion.

JONES, *Circuit Judge*, dissenting:

The construction which the majority of the court place upon Sec. 60 (a) of the Bankruptcy Act, as amended by [fol. 146] the Chandler Act, seems to me to deny the intended effect of the word "antecedent" (as now employed in the Act to define the nature of debt capable of furnishing the basis for a preference) and, at the same time, to give an effect to the provision with respect to the presumed time of transfer under certain specified conditions, contrary to the intent of that provision.

The Chandler Act amendment of Sec. 60 (a) was the first time that the requirement of a debt's antecedency was prescribed by a bankruptcy statute in relation to the establishment of a preference.[1] True enough, such had actually been the law prior to the passage of the Chandler Act, but only by judicial construction. What, therefore, had been the law in material regard, the Chandler Act redeclared by providing in Sec. 60 (a) that "A preference is a transfer

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[1] 3 Collier on Bankruptcy (14th ed.) par. 60.19, p. 818.

* * * of any of the property of a debtor to or for the benefit of a creditor for or on account of an antecedent debt * * * ." The Chandler Act made no new or special definition of "antecedent debt" but left the meaning of that term to the law's prior understanding of it. In these circumstances I am unable to perceive how it can be inferred that Congress intended to transform a debt actually incurred for a present consideration of full value into an antecedent debt simply because a further provision of Sec. 60 (a) postpones to "immediately before bankruptcy" the time of a transfer actually made contemporaneously with the incurrence of the debt but not perfected under local law against a *bona fide* purchaser and creditors of the transferor.

With a preference unqualifiedly defined, as above quoted, as a transfer for an *antecedent* debt (the transferor being insolvent and within four months of bankruptcy), it was then provided by the succeeding sentence of Sec. 60 (a) that "For the purpose of subdivisions a and b of this section, a transfer shall be deemed to have been made at the time when it became so far perfected that no bonafide purchaser from the debtor and no creditor could thereafter [fol. 147] have acquired any rights in the property so transferred superior to the rights of the transferee therein, and, if such transfer is not so perfected prior to the filing of the petition in bankruptcy * * * it shall be deemed to have been made immediately before bankruptcy."

From the foregoing provision the majority conclude (and they have support in the views of learned authors [2]) that "a debt is to be treated as antecedent to a transfer actually made contemporaneously but not perfected as against purchasers and creditors of the debtor until a later time." And so, according to the prevailing argument, the entire transaction of contemporaneous loan and transfer is split

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[2] See McLaughlin, Aspects of the Chandler Bill to Amend the Bankruptcy Act (1937) 4 University of Chicago Law Review 369, 388; Mulder, Ambiguities in the Chandler Act (1940) 89 University of Pennsylvania Law Review, 10, 25; 3 Collier on Bankruptcy (14th ed.) par. 60.48, p. 962 et seq. But see contra 4 Remington on Bankruptcy (4th ed.) § 1717 (text and appendix).

apart and the unperfected[3] transfer is "deemed to have been made immediately before bankruptcy", as Sec. 60 (a) provides, while the loan for which the transfer was contemporaneously made retains the original date of the actual transaction and thus becomes antecedent in relation to the time of the transfer, as statutorily presumed under the attending circumstances. To so hold seems to be a striking instance of lifting oneself by one's bootstraps and terminates in a result which I do not think Sec. 60 (a) was intended to bring about. When the time of the transfer is brought to "immediately before bankruptcy" by virtue of Sec. 60 (a) because of a want of perfection thereof as against a *bona fide* purchaser and creditors of the transferor, the fact as to whether the unperfected transfer was for an antecedent debt or for a debt contemporaneously incurred is still to be reckoned with on the basis of actuality. It will be observed that Sec. 60 (a) does not strike down an unperfected transfer but merely moves, by legal presumption, the time of its occurrence to "immediately before bankruptcy".

In my opinion, the provision in Sec. 60 (a) with respect to the presumed time of transfer under the specified condi- [fol. 148] tions was incorporated in the Chandler Act in order to bring constructively within the four months of bankruptcy (and thus render adjudicable on that basis) all unperfected transfers made while the debtor was insolvent more than four months prior to bankruptcy. Before the Chandler Act, the law did not reach such earlier transfers by an insolvent debtor. But under Sec. 60 (a), as now amended, any unperfected transfer by an insolvent can be assailed as a preference if, when actually made, the consid-

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[3] The term "unperfected" as used herein should not be taken to imply that the assignments in this case were wanting in legal validity. Under local law they were binding and conclusive as to the assignor and its creditors from the time they were made. See Phillips's Estate (No. 4), 205 Pa. 525, 531. They were, moreover, good against the world except that a subsequent bona fide purchaser without notice could have acquired rights in the assigned accounts superior to the rights of the original assignees if he was first to give notice of his acquisition to the persons owing the accounts. It was only to that limited extent that there was any want of perfection in the transfers.

eration therefor was an antecedent debt. So construed, the provision in Sec. 60 (a), relating to the legally presumed time of transfer, works an important change in the law but it has nothing to do with determining the relative date of the incurrence of the debt for which an unperfected transfer was contemporaneously made. Whether the unperfected transfer, when made, was made on account of an antecedent debt or for a present consideration of full money's worth remains the criterion for determining whether the transfer constituted a preference.

What the bankruptcy law is primarily concerned with is the equitable distribution of a bankrupt's estate among creditors. A preference is the favoritism by an insolvent debtor of one creditor over others.[4] But, in order that a payment or transfer by a debtor to one creditor may amount to a preference, it is necessary that the debtor's estate be thereby depleted so that the remaining creditors cannot ratably receive commensurate shares on account of their claims.[5] A transfer therefore which does not reduce the value of a debtor's estate because he contemporaneously receives full value in exchange is not a preference. It is hardly likely that Congress intended by bringing an unperfected transfer to "immediately before bankruptcy" to constitute a preference out of a transaction which in no way depleted the debtor's estate. Bankruptcy does not disapprove of an insolvent debtor's giving security, even down to the date of bankruptcy, for a present loan of full value. [fol. 149] Such action may possibly sustain the breath of fiscal life in a gasping debtor until complete recovery to the ultimate benefit of creditors generally. Indeed, it was in furtherance of that hope that the subject loans in the instant case were given and the transfers made as security therefor. The debtor's estate was in no way depleted but received a needed and desired present benefit. In any view, a contemporaneous transfer in such circumstances is no more a preference under the Chandler Act amendment of Sec. 60 (a) than it was prior to the amendment.

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[4] 3 Collier on Bankruptcy (14th ed.) par. 60.02, pp. 750-751.

[5] See Newport Bank v. Herkeimer Bank, 225 U. S. 178, 184; also 3 Collier on Bankruptcy (14th ed.) par. 60.19, p. 819.

Nor am I able to see how Sec. 60 (a) was intended, as the majority suggest, "to strike down secret liens even though given for a present consideration". The time of the making of a secret lien, if perfected under local law, is no more deemed to have been "immediately before bankruptcy" than is the time of the making of a perfected open lien. And, by the same token, an unperfected open lien is subject to the same limitation under Sec. 60 (a) as is an unperfected secret lien. In no sense does Sec. 60 (a) seek to discriminate between secret and open liens. It simply prescribes the requisites under the bankruptcy law for determining the existence of a preferential transfer. And this, it does without attempting in any way to pass disapprovingly upon what may be a valid (although secret) lien under local law.

The transfers in this case, judged on the basis of having been made "immediately before bankruptcy" (actually they were made within four months of bankruptcy), were valid, having been given as security for debts contemporaneously incurred for full present consideration. Accordingly, I should affirm the order of the District Court.

[fol. 150] IN THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE THIRD CIRCUIT, OCTOBER TERM, 1941

No. 7893

In Re QUAKER CITY SHEET METAL CO., Bankrupt,

Appeal of NORMAN KLAUDER, Trustee

JUDGMENT—August 12, 1942

Appeal from the District Court of the United States, for the Eastern District of Pennsylvania.

This cause came on to be heard on the transcript of record from the District Court of the United States, for the Eastern District of Pennsylvania, and was argued by counsel.

On consideration whereof, it is now here ordered, adjudged, and decreed by this Court that the decree of the said District Court in this cause be, and the same is hereby

reversed, with costs, and the cause is remanded to the said District Court with directions to take such further proceedings as may be consistent with the opinion of this court.

Albert B. Maris, Circuit Judge.

August 12, 1942.

[File endorsement omitted.]

[fol. 151] UNITED STATES OF AMERICA,
Eastern District of Pennsylvania,
Third Judicial Circuit, Set.:

I, Wm. P. Rowland, Clerk of the United States Circuit Court of Appeals for the Third Circuit, Do Hereby Certify the foregoing to be a true and faithful copy of the original Appendix to Brief for Appellant, as constituting the portions of the record before this court at argument; and proceedings in this court in the Matter of Quaker City Sheet Metal Co., Bankrupt, Appeal of Norman Klauder, Trustee, No. 7893, on file, and now remaining among the records of the said Court, in my office.

In Testimony Whereof, I have hereunto subscribed my name and affixed the seal of the said Court, at Philadelphia, this 19th day of September in the year of our Lord one thousand nine hundred and forty-two, and of the Independence of the United States the one hundred and sixty-seventh.

Wm. P. Rowland, Clerk of the U. S. Circuit Court of Appeals, Third Circuit. (Seal.)

[fol. 152] IN THE SUPREME COURT OF THE UNITED STATES,
OCTOBER TERM, 1942

No. —

[Title omitted]

STIPULATION OF COUNSEL PURSUANT TO RULE 38 (8) TO OMIT NON-ESSENTIAL MATTERS FROM PRINTED RECORD

And Now, to wit, this 12th day of September, 1942, It Is Stipulated and Agreed by and between Jenkins, Bennett & Libby, Attorneys for Respondent; and Drinker, Biddle &

Reath, Attorneys for Corn Exchange National Bank and Trust Company, one of the Petitioners; and Saul, Ewing, Remick & Harrison, Attorneys for Edward C. Dearden, Sr., the other Petitioner, that in connection with the Petition for Writ of Certiorari to the Supreme Court of the United States in the above matter, about to be filed by Petitioners, the following portions of the certified transcript of the record in the Circuit Court of Appeals for the Third Circuit shall alone be printed for the uses of the Supreme Court of the United States, the page numbers being the numbers designated on the certified transcript of the typewritten portion of said record in said Circuit Court:

1. The relevant docket entries, appearing at pages 1 and 2, shall be printed.

2. The Petition for Reclamation of Edward C. Dearden, Sr., page 5 to and including page 15, shall be printed, [fol. 153] excluding, however, the affidavit of Edward C. Dearden, appearing on page 9.

3. The Answer of Norman Klauder, Trustee of the Bankrupt Estate, to the Petition for Reclamation, page 20 to and including page 23 shall be printed.

4. The following testimony from the hearing on the claim of Edward C. Dearden, Sr., held on March 27, 1941, shall be printed:

(a) Page 24, line 1, to and through the words "Mr. Mikell:", appearing in the third line from the bottom of page 24.

(b) Page 26, line 15 to the end of said page 26.

(c) Page 27, line 1, to and through line 9 on said page 27.

(d) Page 28, line 4 to and through line 18 on said page 28.

5. The Opinion and Order of the Referee, Henry W. Braude, Esq., sur claim of Edward C. Dearden, Sr., appearing on page 30, shall be printed in its entirety.

6. The following portion of the Proof of Secured Claim of Corn Exchange National Bank and Trust Company shall be printed:

(a) Page 36 to and including line 24 on page 40.

(b) Page 41, line 12 to end of page on page 41, excluding, however, notary's affidavit at bottom of page 41.

(c) Exhibit 1 on page 42 shall be printed, excluding therefrom, however, the entire portion of said Exhibit which is in small type and which begins with the words "including all cash" and ends with the words "protest of this note". This exhibit shall be followed by the following statement: "Exhibits 2, 3, 4 and 5, except for amounts and dates, are substantially identical to Exhibit 1."

[fol. 154] (d) Exhibit 6, appearing on page 44, shall be printed. This Exhibit shall be followed by the following statement: "Exhibits 7 and 8, except for dates and amounts, are substantially identical to Exhibit 6".

(e) Exhibit 9, appearing on page 46, shall be printed, followed by the following statement: "Except for the name of the Purchaser, the nature of the work, and dates, Exhibit 10 is identical to Exhibit 9."

7. The following portions of the notes of testimony at the hearing on the claim of Corn Exchange National Bank and Trust Company, held March 27, 1941, shall be printed:

(a) All of page 51 shall be printed.

(b) Line 19 to the end of page 55 shall be printed.

(c) Line 1 to and including line 16 on page 56 shall be printed.

(d) Line 9 to and including line 23 on page 58 shall be printed.

(e) Line 22 to the end of page 60 shall be printed.

(f) Line 1 on page 61 shall be printed.

(g) The last line on page 61 shall be printed.

(h) Line 1 to and including the words "agreed to", in line 6 on page 62, shall be printed.

(i) Line 24 to the end of page 62 shall be printed.

(j) Line 1 to and including line 3 on page 63 shall be printed.

(k) Line 17 to and including line 22 on page 64 shall be printed.

(l) Line 1 to and including line 21, ending "in business." on page 65, shall be printed.

[fol. 155] (m) Line 13, beginning "Q. And approximately", to and including line 17, on page 66, shall be printed.

(n) Line 22, beginning "Now was there", to the end of page 66, shall be printed.

(o) All of pages 67 and 68 shall be printed.

(p) Line 6, beginning "By Mr. Van Dusen:", to the end of page 69, shall be printed.

(q) All of pages 70, 71 and 72 shall be printed.

(r) Line 1 to and including line 21, ending "is correct", on page 73, shall be printed.

(s) Line 6, beginning "Mr. Bennett:", to and including line 9 on page 74, shall be printed.

(t) Line 12 on page 75, being "By Mr. Van Dusen:", shall be printed.

(u) Line 14, beginning "And all of", to and including line 17 on page 77, shall be printed.

(v) Line 13 on page 79, being "By Mr. Bennett:", shall be printed.

(w) Line 11, beginning "Were the invoices", to and including line 19 on page 80, shall be printed.

(x) Line 19, beginning "Hector A. Sinzheimer having been", to and including line 26, being "1510 Chestnut Street", on page 82, shall be printed.

(y) Line 2, beginning "Mr. Van Dusen:", to and including line 25 on page 83, shall be printed.

8. The entire Opinion and Order of the Referee, Henry W. Braude, Esq., sur claim of Corn Exchange National Bank and Trust Company, appearing on page 93 to and including page 101, shall be printed.

9. Memorandum Order filed September 17, 1941, signed by Judge Kirkpatrick, appearing on page 106, shall be printed.

[fol. 156] 10. Final Decree, filed November 10, 1941, by Judge Kirkpatrick, appearing on page 107, shall be printed in its entirety.

11. All of the proceedings in the Circuit Court of Appeals for the Third Circuit, including the opinion and dissenting opinion of the Judges of the Circuit Court of Appeals for the Third Circuit, shall be printed.

Jenkins, Bennett & Libby, by Bertram Bennett.
Drinker, Biddle & Reath, by Charles J. Biddle.
Saul, Ewing, Remick & Harrison, by Thomas P. Mikell.

[fol. 55] IN THE SUPREME COURT OF THE UNITED STATES,
OCTOBER TERM, 1942

No. —

CORN EXCHANGE NATIONAL BANK AND TRUST COMPANY and Edward C. Dearden, Sr., Petitioners,

vs.

NORMAN KLAUDER, Trustee of the Estate of Quaker City Sheet Metal Co., Bankrupt

AMENDMENT TO STIPULATION OF COUNSEL OMITTING NON-ESSENTIAL MATTERS FROM PRINTED RECORD

And Now, to wit; this 23rd day of September, 1942, It is Stipulated and Agreed by and between Jenkins, Bennett & Libby, Attorneys for Respondent; and Drinker, Biddle & Reath, Attorneys for Corn Exchange National Bank and Trust Company, one of the Petitioners; and Saul, Ewing, Remick & Harrison, Attorneys for Edward C. Dearden, Sr., the other Petitioner, that the Stipulation of Counsel dated September 12, 1942, on file with the Clerk of the Supreme Court of the United States in the above-entitled matter, shall be amended in the following respects:

Paragraph 11 of said Stipulation of Counsel dated September 12, 1942, shall be amended to read as follows:

"11. All of the proceedings in the Circuit Court of Appeals for the Third Circuit, including the opinion and dissenting opinion of the Judges of said Circuit Court of Appeals, shall be printed except the following:

(a) The motion by Corn Exchange National Bank and Trust Company and Edward C. Dearden, Sr., Appellees, to dismiss the appeal, which motion was filed with the Clerk of the Circuit Court on December 10, 1941.

[fol. 56] (b) The amended motion by Corn Exchange National Bank and Trust Company and Edward C. Dearden, Sr., Appellees, to dismiss the appeal, which amended motion was filed with the Clerk of the Circuit Court on December 15, 1941.

(c) Answer of Norman Klauder, Trustee of the Estate of Quaker City Sheet Metal Co., Bankrupt, Appellant, to Appellees' motion to dismiss the appeal.

(d) The order of the Circuit Court of Appeals for the Third Circuit denying the motion of Appellees to dismiss the appeal, which order was filed January 20, 1942.

Jenkins, Bennett & Libby, by Bertram Bennett;
Drinker, Biddle & Reath, by Charles S. Biddle;
Saul, Ewing, Remick & Harrison, by T. P. Mikell.

[fol. 57] SUPREME COURT OF THE UNITED STATES

ORDER ALLOWING CERTIORARI—Filed November 9, 1942

The petition herein for a writ of certiorari to the United States Circuit Court of Appeals for the Third Circuit is granted.

And it is further ordered that the duly certified copy of the transcript of the proceedings below which accompanied the petition shall be treated as though filed in response to such writ.

SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1942

No. 452

CORN EXCHANGE NATIONAL BANK AND TRUST COMPANY, PHILADELPHIA, AND EDWARD C. DEARDEN, SR.,

Petitioners,

vs.

NORMAN KLAUDER, TRUSTEE OF THE ESTATE OF QUAKER CITY SHEET METAL CO., BANKRUPT.

PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE THIRD CIRCUIT.

THOMAS P. MIKELL,
ALLEN S. OLMSTED, 2D,
MAURICE BOWER SAUL,
Counsel for Petitioner Edward C. Dearden, Sr.

CHARLES J. BIDDLE,
JAMES McMULLAN,
Counsel for Petitioner Corn Exchange National Bank and Trust Company.

INDEX.

Subject Index.

Cases Cited.

Statutes Cited.

SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1942

No. 452

CORN EXCHANGE NATIONAL BANK AND TRUST COMPANY, PHILADELPHIA, AND EDWARD C. DEARDEN, SR.,

Petitioners,

vs.

NORMAN KLAUDER, TRUSTEE OF THE ESTATE OF QUAKER CITY SHEET METAL CO., BANKRUPT.

PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE THIRD CIRCUIT.

To the Honorable the Chief Justice and the Associate Justices of the Supreme Court of the United States:

Your Petitioners, Corn Exchange National Bank and Trust Company, Philadelphia, and Edward C. Dearden, Sr., respectfully pray that a writ of certiorari issue to review the judgment and decision of the United States Circuit Court of Appeals for the Third Circuit in the above entitled case, reversing a decision of the United States

District Court for the Eastern District of Pennsylvania, which judgment and decision was rendered by the Circuit Court of Appeals on August 12, 1942.

The appeal in the Circuit Court of Appeals was taken from a decree of the United States District Court for the Eastern District of Pennsylvania, holding that the claim of Corn Exchange National Bank and Trust Company, Philadelphia, one of the Petitioners, be allowed as a secured claim in the sum of $7,954.51, and that the claim of Edward C. Dearden, Sr. should be allowed as a secured claim in the sum of $1,550, against the Estate of Quaker City Sheet Metal Co., Bankrupt.

Statement of the Matter Involved.

This case involves the proper interpretation of the new provisions added by the Chandler Act of 1938 to the preference section (Section 60 (a)) [1] of the Bankruptcy Act.

The facts are not in dispute (R. 13, 24). Quaker City Sheet Metal Company (hereinafter called the "Bankrupt"), acting under the supervision of a Creditors' Committee (R. 6, 26, 33) made an arrangement with Corn Exchange National Bank and Trust Company, Philadelphia, one of the Petitioners (hereinafter called the "Bank"), whereby the Bank loaned money to Bankrupt from time to time upon the security of contemporaneous assignments of accounts receivable (R. 18, 32, 34). This arrangement was carried out from May, 1938 until the date of bankruptcy. In addition, certain new contracts were negotiated by the Bankrupt (R. 29, 30). The Bank advanced money to meet payrolls under an agreement giving the Bank an assignment of moneys due and to become due under the contracts (R. 30). As the moneys became due they were again

[1] Act of June 22, 1938 (52 Stat. 869, U. S. C., Title 11, Section 96).

assigned to the Bank and the assignment was noted on copies of invoices (R. 28, 30).

Notice of the aforementioned assignments was not given the obligors of the accounts receivable and moneys due and to become due under the contracts (R. 25, 34). As of the date of bankruptcy there was due the Bank on account of all of the above transactions the principal sum of $7,954.51 (R. 15).

In addition to the above, the Bankrupt obtained from Edward C. Dearden, Sr., one of the Petitioners herein, a loan of $1,550, secured by the contemporaneous assignment of a contract between Bankrupt and York Ice Machinery Company and any moneys due or to become due thereunder (R. 2, 6, 10).

No notice, however, was given to York Ice Machinery Company of this assignment (R. 12, 13, 14).

After the filing on April 15, 1940, of the involuntary petition in bankruptcy, the Bank filed its claim as a secured creditor in the sum of $7,954.51 (R. 15), and Dearden, Sr. filed a petition for reclamation of the sum of $1,550 from the proceeds of the York Ice Machinery contract (R. 2).

The Trustee recognized that the aforementioned assignments were made as security for contemporaneous loans, but resisted Petitioners' claims on the basis of the wording of the second sentence of Section 60 (a) of the Chandler Act. The clause he relied on provides that

> "a transfer shall be deemed to have been made at the time when it became so far perfected that no bona fide purchaser from the debtor and no creditor could thereafter have acquired any rights in the property so transferred superior to the rights of the transferee therein . . . ."

This provision, the trustee contended, had effected a change in the previously accepted view of a preference. A bona fide purchaser of the receivable, it was argued, *could* have acquired a right in it superior to the Bank's right by notifying the obligor of the receivable. Therefore the transfer had not been perfected. Therefore it must be deemed to have been made at a date after it was actually made. Therefore the consideration for the transfer, although actually given contemporaneously with the transfer, must be deemed to be antecedent to the transfer. Therefore, it is an antecedent debt, and therefore a preference. Thus the reasoning of the trustee.

Referee in Bankruptcy Henry W. Braude on April 21, 1941, allowed the claims of the Bank and of Edward C. Dearden, Sr. (R. 38, 14). The United States District Court for the Eastern District of Pennsylvania, by Kirkpatrick, J., affirmed the Referee's orders (R. 38). Respondent herein then appealed to the United States Circuit Court of Appeals for the Third Circuit, which, by an opinion filed August 12, 1942 (R. 41), (Judge Jones dissenting, R. 46), reversed the decree of the District Court (R. 46). The holding of the Circuit Court was to the effect that the Chandler Act had changed the law, and, because of the failure to give notice, the assignment to Petitioners of the accounts receivable and moneys due and to become due under the contracts constituted a preference within the meaning of the Bankruptcy Act, as amended.

Jurisdiction.

The jurisdiction of this Court is invoked under Section 240 (a) of the Judicial Code, as amended by the Act of February 13, 1925 (43 Stat. 938, U. S. C., Title 28, Section 347), and Section 24 (c) of the Bankruptcy Act of June 22,

1938. (52 Stat. 854, U. S. C., Title 11, Section 47). The judgment of the United States Circuit Court of Appeals for the Third Circuit to be reviewed was entered on August 12, 1942.

Questions Involved.

1. Whether the Chandler Act of 1938 (Section 60 (a) of the Bankruptcy Act as amended) has changed the prior definition of a preference so as to include a transfer of property for a present adequate consideration, when a step in the perfection of the transfer (in this case the notification to the obligor of the assignment of accounts receivable and moneys due and to become due under contracts) is taken after the transfer itself and the payment therefor.

2. Whether notice to the obligor of the accounts receivable and moneys due and to become due under a contract is a necessary step in the perfection of the transfer of such property, within the meaning of Section 60 (a) of the Chandler Act.

Reasons Relied on For Allowance of Writ.

In holding that a transfer of accounts receivable and moneys due and to become due under contracts made contemporaneously with and as security for a loan, is to be deemed as a transfer for or on account of an antecedent debt because of the lender's failure to give notice to the obligors, and thus preferential within the meaning of Section 60 (a) of the Bankruptcy Act, the Circuit Court of Appeals for the Third Circuit

1. Has rendered a decision which the Circuit Court itself (R. 44) recognizes is in conflict with the decision of the United States Circuit Court of Appeals for the

Fifth Circuit in *Adams* v. *City Bank & Trust Co.*, 115 Fed. (2d) 453, decided on November 12, 1940 (cert. denied by this Court, 312 U. S. 699).

2. Has decided an important question of Federal law which has not been but should be settled by this Court, in that it interprets the 1938 amendment to the Bankruptcy Act, as changing the concept of preferences so as to make the question of preference turn, not on whether the consideration for the transfer is present or antecedent, but on whether the transfer is technically perfected at the very moment the consideration passes.

3. Has divided in its opinion, in that two Judges (Maris and Goodrich JJ.) voted for reversal, and one Judge (Jones, J.) voted for affirmance.

4. Has decided an important question of local law relating to the effectiveness of an assignment without notice, in a way probably in conflict with applicable local decisions.

Wherefore, your Petitioners respectfully pray that a writ of certiorari be issued out of and under the seal of this Court, directed to the United States Circuit Court of Appeals for the Third Circuit, sitting at Philadelphia, Pennsylvania, commanding that Court to certify and to send to this Court on a day certain to be therein named a full and complete transcript of the record and all proceedings had in this case numbered and entitled on its docket 7893 to the end that this case may be reviewed and determined by this Court; that the said judgment of the United States Circuit Court of Appeals for the Third Circuit may be reversed by this Court; and that your Petitioners may have such other

and further relief in the premises as may seem just and proper.

And your Petitioners will ever pray, etc.

Edward C. Dearden, Sr.,
By Thomas P. Mikell,
Allen S. Olmstead, 2d,
Maurice Bower Saul,
Packard Building,
15th & Chestnut Streets,
Philadelphia, Pa.,
Attorneys for Edward C. Dearden, Sr.,
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Saul, Ewing, Remick & Harrison,
Of Counsel.

Corn Exchange National Bank and Trust Company, Philadelphia,
By Charles J. Biddle,
James McMullan,
1429 Walnut Street,
Philadelphia, Pa.,
Attorneys for Corn Exchange National Bank and Trust Company, Philadelphia,
One of Petitioners.

Drinker, Biddle & Reath,
Of Counsel.

BRIEF IN SUPPORT OF PETITION.

Opinions Below.

The opinions of the Referee appear in the Record at pages 14 and 32. The memorandum opinions of the District Court appear in the Record at pages 38 and 39. The opinion of the Circuit Court of Appeals for the Third Circuit appears in the Record at page 41, the dissenting opinion at page 46. None of the foregoing opinions have yet been reported in official reports, except that of the Circuit Court of Appeals, which is reported in 129 Fed. (2d) 824.

Jurisdiction.

The grounds on which jurisdiction of this Court is invoked are set forth in the Petition at pages 4-5 thereof.

Statement of the Case.

The Statement of the Case appears in the Petition at pages 2 to 4, and in the interest of brevity is not repeated herein.

Specification of Errors.

The errors which Petitioners will urge if the writ of certiorari be granted are that the Circuit Court of Appeals for the Third Circuit erred:

1. In holding that where a transfer is made as security for a contemporaneous debt, the same will be deemed to have been made for or on account of an antecedent debt so as to constitute a preference within the meaning of the new provisions of Section 60 (a) of the Bankruptcy Act, if the transfer was not so far technically perfected at the

time the loan was made that no bona fide purchaser from or creditor of the debtor could have acquired any rights in the transferred property superior to the transferee, which holding is erroneous for the following reasons:

(a) The amendment to Section 60 (a) of the Bankruptcy Act does not purport to change the prior rule that a transfer of property by a debtor as security for a contemporaneous loan is not a transfer for or on account of an antecedent debt; compare Section 60 (b).

(b) Section 60 (a) does not purport to change the prior rule and invalidate a transfer which has caused no diminution of the bankrupt estate.

(c) Section 60 (a) does not purport to give the Trustee the status of a bona fide purchaser; sections 70 (a) and (c) of the Bankruptcy Act indicate that Congress did not purport to change the prior law on this question.

(d) The interpretation of the Circuit Court of Appeals creates an unreasonable inconsistency between Section 60 (a) and Section 70 (d), which validates transfers made in good faith after bankruptcy for a present consideration and before adjudication or possession taken.

2. In holding that under the law of Pennsylvania and the Bankruptcy Act, the transfer of a contract right is not perfected as against the Trustee in Bankruptcy of the transferrer until notice of the transfer is given to the obligor.

Statute Involved.

The applicable provision of the Bankruptcy Act of June 22, 1938, is est forth in the Appendix, *infra*, page 14.

Argument.

This case involves the question whether Congress by its amendment to Section 60 (a) of the Bankruptcy Act, has done away with the prior concept that a preference will never result if present adequate consideration is given for a transfer. The Circuit Court of Appeals for the Third Circuit held that a preference will result where the transfer is not technically and completely perfected at the time the loan is made, even though it be for a present adequate consideration.

The first sentence of the amended Section 60 (a) states that a preference must involve a transfer "for or on account of an antecedent debt". The Circuit Court of Appeals held that, because of the new addition of the second sentence to this section, a transfer, although actually made at the same time a loan is made, will be deemed to have been made subsequent to the loan (and thus for an antecedent debt) if the transfer at the moment it is made is not so far technically perfected that thereafter no bona fide purchaser from or creditor of the transferrer *could* acquire any rights superior to the transferee.

This conclusion, it is submitted, gives a broader significance to Section 60 (a) than was intended by Congress. The new amendment was intended to eliminate the inequity which formerly arose where, for example, a transfer was made for or on account of a preexisting debt and then the transfer was perfected by recording within four months of bankruptcy. Under the prior law, such recording related back to the date of the assignment (i. e., more than four months before bankruptcy) and the transfer, even though for an antecedent debt, was permitted to stand as against the Trustee. Under the amended Section 60, this situation

can no longer exist. Congress did not intend to invalidate transfers made for an adequate present consideration.

The decision of the Circuit Court of Appeals in this case is in direct conflict with and diametrically opposed to the decision of the Circuit Court of Appeals for the Fifth Circuit in *Adams* v. *City Bank and Trust Company*, 115 F. (2d) 453, decided on November 12, 1940. That Circuit Court of Appeals held that the new provisions of Section 60 (a) do not make a preference out of a transfer entered into for an adequate present consideration, although the transfer is not perfected until subsequently (in that case by recording) while the debtor is insolvent and less than four months before the bankruptcy. The Circuit Court of Appeals in the present case recognizes that its decision is in conflict with the holding in the above case (R. 44).

The question whether the Chandler Act has changed the concept of a preference, particularly with reference to assignments of accounts receivable, has invoked considerable discussion, but has not been decided by this Court. Authorities are divided.[2]

It is significant that if the Circuit Court of the Third Circuit is correct in its interpretation of Section 60 (a), then a lender can never be certain that his security is safe, unless it is clear that the transfer is effective so that under the laws of all of the states of this country, and all the countries of the world, no one *could* obtain a superior right.

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[2] See: 4 *Remington on Bankruptcy* (4th Ed.) Sec. 1717; *Neyhoff, Assignment of Accounts Receivable as Affected by the Chandler Act*, 34 Ill. Law Review 538 (1940); *Hamilton, The Effect of Section 60 of the Bankruptcy Act upon Assignments of Accounts Receivable*, 26 Va. Law Review 168 (1939); *Kach, Transfers of Non-Negotiable Accounts and the Chandler Act*, 46 Commercial L. J. 133 (1941); *Compare: McLaughlin, Aspects of the Chandler Bill to Amend the Chandler Act*, 4 U. of Chic. L. Rev. 369, 388 (1937); *Mulder, Ambiguities in the Chandler Act*, 89 U. of Pa. L. Rev. 10, 25 (1940); 3 *Collier on Bankruptcy* (14th Ed.) Sec. 60.48.

In addition to the above, it is submitted that the Circuit Court of Appeals for the Third Circuit has misinterpreted *Phillips' Estate #4*, 205 Pa. 525. The latter decision held that notice is not necessary in order to perfect an assignment of a contract right, although failure to give notice may result in other persons acquiring superior equities.

The *Pennsylvania Act of July 31, 1941*, P.L. 606, 69 Pa. Purdon's Statutes, Section 561, which dispenses with the necessity of giving notice in Pennsylvania of an assignment of accounts receivable, but which was not applicable to the present case, does not make the question moot in Pennsylvania. If the Circuit Court is correct, then, in spite of the Act of 1941, it is possible that a subsequent bona fide purchaser in another state, having a different law, *could* acquire a better title to accounts receivable owing to a creditor in Pennsylvania. Moreover, the same interpretation of the Chandler Act would apply to conditional sales, bailment leases and other forms of collateral not mentioned in the 1941 act.

The question involved here is of great and imminent importance to the commercial world, for it goes to the very root of lending money on the security of contemporaneous assignments. Unless banks and other lending institutions can be assured that such loans will not be deemed preferences under Section 60 (a) as amended, they will be unable safely to engage in the fundamental practice of lending money on the security of assignments of many types of personal property. Its bearing on the financing of war contracts is obvious.

Conclusion.

It is, therefore, respectfully submitted that, for the foregoing reasons, this Court should grant the Petition for Certiorari.

Respectfully submitted,

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APPENDIX.

Bankruptcy Act of 1938 (Chandler Act):

SEC. 60. PREFERRED CREDITORS.—a. A preference is a transfer, as defined in this Act, of any of the property of a debtor to or for the benefit of a creditor for or on account of an antecedent debt, made or suffered by such debtor while insolvent and within four months before the filing by or against him of the petition in bankruptcy, * * * the effect of which transfer will be to enable such creditor to obtain a greater percentage of his debt than some other creditor of the same class. For the purposes of subdivisions a and b of this section, a transfer shall be deemed to have been made at the time when it became so far perfected that no bona fide purchaser from the debtor and no creditor could thereafter have acquired any rights in the property so transferred superior to the rights of the transferee therein, and, if such transfer is not so perfected prior to the filing of the petition in bankruptcy * * * it shall be deemed to have been made immediately before bankruptcy.

b. Any such preference may be avoided by the trustee if the creditor receiving it or to be benefitted thereby or his agent acting with reference thereto has, at the time when the transfer is made, reasonable cause to believe that the debtor is insolvent. Where the preference is voidable, the trustee may recover the property or, if it has been converted, its value from any person who has received or converted such property, except a bona fide purchaser from or lienor of the debtor's transferee for a present fair equivalent value: PROVIDED, HOWEVER, That where such purchaser or lienor has given less than such value, he shall nevertheless have a lien upon such property, but only to the extent of the consideration actually given by him. Where a preference by way of lien or security title is voidable, the court may on due notice order such lien or title to be preserved for the benefit of the estate, in which event such lien or title shall pass to the trustee * * *.

c. If a creditor has been preferred, and afterward in good faith gives the debtor further credit without security

of any kind for property which becomes a part of the debtor's estate, the amount of such new credit remaining unpaid at the time of the adjudication in bankruptcy may be set off against the amount which would otherwise be recoverable from him.

* * * * * * *

SEC. 70. TITLE TO PROPERTY.—a. The trustee of the estate of a bankrupt * * * shall * * * be vested by operation of law with the title of the bankrupt as of the date of the filing of the petition in bankruptcy * * * to all (1) documents relating to his property; (2) interests in patents, patent rights, copyrights, and trade-marks, and in applications therefor: * * * (3) powers which he might have exercised for his own benefit, but not those which he might have exercised solely for some other person; (4) property transferred by him in fraud of his creditors; (5) property, including rights of action, which prior to the filing of the petition he could by any means have transferred, or which might have been levied upon and sold under judicial process against him, or otherwise seized, impounded, or sequestered: * * * (6) rights of action arising upon contracts, or usury, or the unlawful taking or detention of or injury to his property; (7) contingent remainders, executory devises and limitations, rights of entry for condition broken, rights or possibilities of reverter, and like interests in real property, * * * and (8) property held by an assignee for the benefit of creditors * * *. All property which vests in the bankrupt within six months after bankruptcy by bequest, devise, or inheritance shall vest in the trustee * * *. All property in which the bankrupt has at the date of bankruptcy an estate or interest by the entirety and which * * * becomes transferable * * * solely by the bankrupt shall * * * vest in the trustee * * *.

c. * * * The trustee, as to all property in the possession or under the control of the bankrupt at the date of bankruptcy or otherwise coming into the possession of the bankruptcy court, shall be deemed vested as of the date of bankruptcy with all the rights, remedies, and powers of a

creditor then holding a lien thereon by legal or equitable proceedings, whether or not such a creditor actually exists; and, as to all other property, the trustee shall be deemed vested as of the date of bankruptcy with all the rights, remedies, and powers of a judgment creditor then holding an execution duly returned unsatisfied, whether or not such a creditor actually exists.

d. After bankruptcy and either before adjudication or before a receiver takes possession of the property of the bankrupt, whichever first occurs—

(1) A transfer of any of the property of the bankrupt, other than real estate, made to a person acting in good faith shall be valid against the trustee if made for a present fair equivalent value or, if not made for a present fair equivalent value, then to the extent of the present consideration actually paid therefor, for which amount the transferee shall have a lien upon the property so transferred; . . .

IN THE

Supreme Court of the United States

October Term, 1942.

No. 452.

CORN EXCHANGE NATIONAL BANK AND TRUST COMPANY, PHILADELPHIA, and EDWARD C. DEARDEN, SR.,

Petitioners,

v.

NORMAN KLAUDER, Trustee of the Estate of QUAKER CITY SHEET METAL CO., Bankrupt,

Respondent.

On Writ of Certiorari to the United States Circuit Court of Appeals for the Third Circuit.

BRIEF FOR PETITIONERS.

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International, 236 Chestnut St., Philadelphia

INDEX TO BRIEF FOR PETITIONERS.

TABLE OF CASES CITED.

AUTHORITIES AND REPORT CITED.

STATUTES CITED.

Page

Bankruptcy Act:

Section 60.

Act July 1, 1898, c. 541, 30 Stat. 562 ..... 11, 37
Act February 5, 1903, c. 487, 32 Stat. 799 .. 11, 16, 37
Act June 25, 1910, c. 412, 36 Stat. 842 ..... 11, 38
Act May 27, 1926, c. 406, 44 Stat. 666 ..... 11, 38
Act June 22, 1938, c. 575, 52 Stat. 869; 11 U. S. C. A. Sec. 96 .... 2, 4, 5, 6, 7, 8, 10, 12, 13, 17, 18, 20, 22, 24, 25, 26, 27, 28, 30, 33, 34, 39

Section 24 (c).

Act June 22, 1938, 52 Stat. 854, 11 U. S. C. A. Sec. 47 2

Section 70.

Act June 22, 1938, c. 575, 52 Stat. 879, 11 U. S. C. A. Sec. 110 ..... 6, 14, 30, 31

Section 1.

Act June 22, 1938, c. 575, 52 Stat. 840, 11 U. S. C. A. Sec. 1 10

Section 67 (d).

Act June 25, 1910, 36 Stat. 842, 11 U. S. C. A. Sec. 107 (d) 17

Judicial Code:

Section 240 (a): Act February 13, 1925, 43 Stat. 938, 28 U. S. C. A. Sec. 347 2

Bankruptcy Act of 1867:

14 Stat. 517 16

Pennsylvania Assignment of Accounts Receivable Act:

Act July 31, 1941, P. L. 606, 69 Purd. Stats. Sec. 561. 30

IN THE

Supreme Court of the United States.

No. 452. October Term, 1942.

CORN EXCHANGE NATIONAL BANK AND TRUST COMPANY, PHILADELPHIA, AND EDWARD C. DEARDEN, SR.,

Petitioners,

v.

NORMAN KLAUDER, TRUSTEE OF THE ESTATE OF QUAKER CITY SHEET METAL CO., BANKRUPT,

Respondent.

ON WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE THIRD CIRCUIT.

BRIEF FOR PETITIONERS.

This case comes before the Court on Writ of Certiorari issued to review a decree of the United States Circuit Court of Appeals for the Third Circuit.

OPINIONS BELOW.

The opinions and orders of the Referee, Henry W. Braude, Esq., filed on April 21, 1941, appear in the Record at pages 14 and 32. The opinions and order of the United States District Court for the Eastern District of Pennsylvania by District Judge Kirkpatrick, filed September 17, and November 10, 1941, appear in the Record at pages 38 and 39.

The opinion of the United States Court of Appeals for the Third Circuit, written by Circuit Judge Maris, and concurred in by Circuit Judge Goodrich (R. 41), with a dissent written by Circuit Judge Jones (R. 46) was filed on August 12, 1942, and is reported in 129 Fed. (2d) 894.

JURISDICTION.

The jurisdiction of this Court to review the judgment of the Circuit Court of Appeals for the Third Circuit on a Writ of Certiorari is provided by Section 240 (a) of the Judicial Code, as amended by the Act of February 13, 1925 (43 Stat. 938, 28 U. S. C. A. Sec. 347) and Section 24 (c) of the Bankruptcy Act of June 22, 1938 (52 Stat. 854, 11 U. S. C. A. Sec. 47).

The judgment of the United States Circuit Court of Appeals for the Third Circuit was entered August 12, 1942 (R. 50). Petition for Writ of Certiorari was granted by this Court on November 9, 1942 (R. 55).

STATEMENT OF THE CASE.

This case involves the proper interpretation of the new provisions added by the Chandler Act of 1938 to the preference section (Section 60 (a))[1] of the Bankruptcy Act.

The facts are not in dispute (R. 13, 24). Quaker City Sheet Metal Company (hereinafter called the "Bankrupt"), acting under the supervision of a Creditors' Committee (R. 6, 26, 33) made an arrangement with Corn Exchange National Bank and Trust Company, Philadelphia, one of the Petitioners, Appellants herein, (hereinafter called the "Bank"), whereby the Bank loaned money to

[1] Act of June 22, 1938, c. 575, Sec. 1, 52 Stat. 869, 11 U. S. C. A. Sec. 96.

Bankrupt from time to time upon the security of contemporaneous assignments of accounts receivable (R. 18, 32, 34). This arrangement was carried out from May 1938 until the date of bankruptcy on April 15, 1940. In addition, certain new contracts were negotiated by the Bankrupt (R. 29, 30). The Bank advanced money to meet payrolls under an agreement giving the Bank an assignment of moneys due and to become due under the contracts. (R. 30.) The assignments were noted upon the books of the bankrupt and were stamped upon its ledgers (R. 28). As the moneys became due they were again assigned to the Bank and the assignment was noted on the copies of the invoices retained by the Bankrupt (R. 28, 30). All of the assignments were made with the express approval of the Creditors' Committee representing approximately 80% of the unsecured creditors and were in fact signed by the Chairman of the Committee (R. 26, 29, 30).

Notice of the aforementioned assignments was not given the obligors of the accounts receivable and moneys due and to become due under the contracts (R. 25, 34). As of the date of bankruptcy there was due the Bank on account of all of the above transactions the principal sum of $7,954.51 (R. 15).

In addition to the above, the Bankrupt obtained on April 12, 1940, from Edward C. Dearden, Sr., one of the Petitioners herein, a loan of $1,550, secured by the contemporaneous assignment of a contract between Bankrupt and York Ice Machinery Company and any moneys due or to become due thereunder (R. 2, 6, 10).

No notice, however, was given to York Ice Machinery Company of this assignment (R. 12, 13, 14).

After the filing on April 15, 1940, of the involuntary petition in bankruptcy, the Bank filed its claim as a secured

creditor in the sum of $7,954.51 (R. 15), and Dearden, Sr. filed a petition for reclamation of the sum of $1,550 from the proceeds of the York Ice Machinery contract (R. 2).

The Trustee recognized that the aforementioned assignments were made as security for contemporaneous loans, but resisted Petitioners' claims on the basis of the wording of the second sentence of Section 60 (a) of the Chandler Act. The clause he relied on provides that

> "a transfer shall be deemed to have been made at the time when it became so far perfected that no bona fide purchaser from the debtor and no creditor could thereafter have acquired any rights in the property so transferred superior to the rights of the transferee therein * * *"

This provision, the trustee contended, had effected a change in the previously accepted view of a preference. A hypothetical bona fide purchaser of the receivable, it was argued, *could* have acquired a right in it superior to the Bank's right by notifying the obligor of the receivable. Therefore the transfer had not been perfected. Therefore it must be deemed to have been made at a date after it was actually made. Therefore the consideration for the transfer, although actually given contemporaneously with the transfer, must be deemed to be antecedent to the transfer. Therefore, it is an antecedent debt, and therefore a preference. Thus the reasoning of the trustee.

Referee in Bankruptcy Henry W. Braude on April 21, 1941, allowed the claims of the Bank and of Edward C. Dearden, Sr. (R. 38, 14). The United States District Court for the Eastern District of Pennsylvania, by Kirkpatrick, J., affirmed the Referee's orders (R. 38). Respondent

herein then appealed to the United States Circuit Court of Appeals for the Third Circuit, which, by an opinion filed August 12, 1942 (R. 41), (Judge Jones dissenting, R. 46), reversed the decree of the District Court (R. 46). The holding of the Circuit Court was to the effect that the Chandler Act had changed the law, and, because of the failure to give notice, the assignment to Petitioners of the accounts receivable and moneys due and to become due under the contracts constituted a preference within the meaning of the Bankruptcy Act, as amended.

SPECIFICATION OF ERRORS INTENDED TO BE URGED.

The Petitioners intend to urge the following assigned errors:

That the Circuit Court of Appeals for the Third Circuit erred:

1. In holding that where a transfer is made as security for a contemporaneous debt, the same will be deemed to have been made for or on account of an antecedent debt so as to constitute a preference within the meaning of the new provisions of Section 60 (a) of the Bankruptcy Act, if the transfer was not so far technically perfected at the time the loan was made that no bona fide purchaser from or creditor of the debtor could have acquired any rights in the transferred property superior to the transferee, which holding is erroneous for the following reasons:

(a) The amendment to Section 60 (a) of the Bankruptcy Act does not purport to change the prior rule that a transfer of property by a debtor as security for a contemporaneous loan is not a

transfer for or on account of an antecedent debt; compare Section 60 (b).

(b) Section 60 (a) does not purport to change the prior rule and invalidate a transfer which has caused no diminution of the bankrupt estate.

(c) Section 60 (a) does not purport to give the Trustee the status of a bona fide purchaser; sections 70 (a) and (c) of the Bankruptcy Act indicate that Congress did not purport to change the prior law on this question.

(d) The interpretation of the Circuit Court of Appeals creates an unreasonable inconsistency between Section 60 (a) and Section 70 (d), which validates transfers made in good faith after bankruptcy for a present consideration and before adjudication or possession taken.

QUESTIONS PRESENTED.

1. Whether the Chandler Act of 1938 (Section 60 (a) of the Bankruptcy Act, as amended) has changed the prior definition of a preference so as to include a transfer of an account receivable for a present adequate consideration, where no notice is given to the debtor.

2. Whether the second sentence of Section 60 (a) of the Bankruptcy Act, as amended by the Chandler Act, fixing the time at which a transfer is deemed to have been made, has the effect of transforming, by a legal fiction, a transfer for a present consideration into a transfer for an antecedent debt.

SUMMARY OF ARGUMENT.

Under a proper construction of Section 60 (a) of the Bankruptcy Act as amended, a bona fide transfer for a present adequate consideration cannot result in a preference. This is borne out by a consideration of the new amendments to Section 60 (a), by the history of the prior provisions of Section 60 (a) and of other provisions in the Bankruptcy Act. All of the lower Courts which have considered the present question, except the Court below in this case, have reached the conclusion contended for by Petitioners.

ARGUMENT.

The facts not being in dispute, the question is purely one of the proper legal interpretation of Section 60 (a) of the Bankruptcy Act, which provides as follows:

> "A preference is a transfer, as defined in this Act, of any of the property of a debtor to or for the benefit of a creditor for or on account of an antecedent debt made or suffered by such debtor while insolvent and within four months before the filing by or against him of the petition in bankruptcy . . . the effect of which transfer will be to enable such creditor to obtain a greater percentage of his debt than some other creditor of the same class. For the purposes of subdivisions (a) and (b) of this section, a transfer shall be deemed to have been made at the time when it became so far perfected that no bona fide purchaser from the debtor and no creditor could thereafter have acquired any rights in the property so transferred superior to the rights of the transferee therein, and, if such transfer is not so perfected prior to the filing of the petition in bankruptcy . . . it shall be deemed to have been made immediately before bankruptcy."

A Transfer for a Present Consideration by Its Very Nature Can Never Be a Preference.

Before it is possible to have a preference, it would seem obvious that someone, who should share equally with another in the assets of the bankrupt, must get more than his fair share. The word "preference" imports the relation of existing creditors having equal equities at the time of the transfer, whereby the rights of one are advanced over those of another. When full value is given for the thing transferred by the bankrupt, clearly the bankrupt has just as much as he had before the transfer and no one has

been injured. The decision of the Circuit Court of Appeals in this case is that despite the fact that the petitioners made loans to the Quaker City Sheet Metal Company at the time that they received the collateral of the assigned accounts, nevertheless they must give up their rights against the collateral and be treated as general creditors. It would be just as logical to say that if they had bought something from the bankrupt at its fair value, they must return it and be relegated to the position of general creditors with respect to their claims to receive back the purchase price paid. There is no essential difference between the two transactions so far as the rights of the claimants against the bankrupt estate are concerned. Neither the lender on collateral nor the outright purchaser is the owner of any claim at the time of the transfer. Both the lender and the purchaser received something from the bankrupt by virtue of the transfer, for which they at the same time paid full value, so that there can be no depletion of the bankrupt's estate at the expense of the general creditors. Where a loan is made and secured by collateral contemporaneously given, the fundamental essential of a preferential transfer is lacking. "The mortgage was not voidable as a preference under § 60b. Preference implies paying or securing a pre-existing debt of a person preferred.": *Dean v. Davis*, 242 U. S. 438, 443 (1917). "A preference presupposes some credit given, a period when the debt existed unsecured; there can be none when the debt is secured as soon as it becomes a debt.": *Ross v. Francis*, 72 Fed. (2d) 358 (C. C. A. 2, 1934).

The object of prohibiting preferences is of course to prevent favoritism among those of the debtor's creditors who ought in fairness to stand on the same footing. It is a

necessary corollary that before such favoritism can exist the transfer must result in a depletion of the estate.

The first sentence of Section 60 (a) clearly states that a preference must involve a transfer "*to or for the benefit of a creditor for or on account of an antecedent debt*". The effect of the transfer must be to enable the creditor to obtain a greater slice of his debt than some other creditor of the same class. The definition of a creditor in Section 1, subsection (11) provides:

> "'Creditor' shall include anyone who owns a debt, demand or claim provable in bankruptcy, . . ."[1]

Since in the present case the transfers of the assigned accounts were made in consideration of contemporaneous loans by the petitioners, it is obvious that they were not creditors within the meaning of Section 60 (a) for the simple reason that they did not then own any debt provable in bankruptcy. Hence, they could not possibly have been in the "same class" with the unsecured creditors whom the Trustee represents.

History of Section 60.

The history of Section 60 of the Act clearly demonstrates that it has not now and never has had anything to do with transfers contemporaneous with loans to the bankrupt. The Section has been several times amended but always these amendments have been for the purpose of clarifying, with relation to the four months' period, the time at which a transfer for an *antecedent debt* became perfected. The first amendment to the 1898 Bankruptcy

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[1] Act of June 22, 1938, c. 575, Sec. 1, 52 Stat. 840, 11 U. S. C. A., Sec. 1.

Act[1] was made in 1903. This amendment[2] provided that, if recording of a transfer was required, the four months' period was prolonged or delayed until the transfer was in fact recorded. Nevertheless, the Courts subsequently held that the time of recording as distinguished from the date of the transfer, did not necessarily furnish the criterion as to the preferential character of the transfer. *In re Watson*, 201 Fed. 962 (D. C. Ky., 1912), aff. 216 Fed. 483, Appeal dism. 239 U. S. 656; *In re Sturtevant*, 188 Fed. 196 (C. C. A. 7, 1911). In 1910 another amendment[3] was passed making a transfer voidable if recording is required and if at the time of the recording the bankrupt was insolvent. In 1926 Section 60 (a) was again amended[4] so as to make it apply to cases where recording was *permitted* as well as to cases where recording was *required* by law. However, Section 60 (b) relating to voidable preferences was not amended at that time and consequently a controversy arose as to whether the preference was voidable where the recording was permitted but not required.

The apparent purpose of the present amendment was to make transfers voidable which either can or should be perfected, if they are not in fact perfected within four months of bankruptcy or at a time when the bankrupt was solvent, *provided always that the transfers were for or on account of an antecedent debt.* In every case it is first necessary to determine *whether there has been a preference*, and unless there has been, we never reach the second

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[1] Act of July 1, 1898, C. 541, Sec. 60, 30 Stat. 562.
[2] Act of Feb. 5, 1903, C. 487, Sec. 13, 32 Stat. 799.
[3] Act of June 25, 1910, C. 412, Sec. 11, 36 Stat. 842.
[4] Act of May 27, 1926, C. 406, Sec. 14, 44 Stat. 666.

question under Section 60, namely, *whether such preference is illegal and may be set aside.*

An examination of the original Act and its amendments shows that in all of them the definition of a preference contains the fundamental that *the effect must be that one creditor is enabled to obtain a greater percentage of his debt than some other creditor of the same class.* See the Appendix to this brief, in which the text of the original Act and the various amendments is given, the requirement of Section 60 (a) that the effect of a preference must be to give one creditor a greater percentage of his debt than another creditor of the same class being italicized in each case.

It is therefore clear that the Chandler Amendment of 1938 to Section 60 of the Bankruptcy Act was not intended to affect transfers made for a present consideration. The purpose was simply to eliminate the situation which formerly arose *where a transfer was made for or on account of an antecedent debt*, and then the transfer was recorded within four months of bankruptcy. Under the previous law where the recording statute was permissive and not mandatory, such recording related back to the date of the assignment (i. e., more than four months before bankruptcy) and the transfer, even though for an antecedent debt, was permitted to stand as against the Trustee in Bankruptcy. Under Section 60, as amended by the Chandler Act, this can no longer occur.

Validity of Transfers for Value Is Recognized Throughout the Act.

There is nothing in the Chandler Act amendments to indicate that Congress intended to change the basic conception of a preference or to affect transfers made *at any*

time for a present consideration. In fact, an examination of the Act as a whole shows exactly the contrary.

Subsection (b) of Section 60 provides:

> "Where the preference is voidable, the trustee may recover the property, or, if it has been converted, its value, from any person who has received or converted such property, *except a bona fide purchaser from or lienor of the debtor's transferee for a present fair equivalent value: Provided, however, that where such purchaser or lienor has given less than such value, he shall nevertheless have a lien upon such property, but only to the extent of the consideration actually given by him.*" (Emphasis supplied.)

Certainly Congress never intended that a bona fide purchaser from one who had received a voidable preference should be able to retain that which he received to the extent that he gave value for it, but at the same time one who had bona fide and in good faith given value directly to the bankrupt should be relegated to the position of a general creditor.

Subsection (c) of Section 60 provides:

> "If a creditor has been preferred, and afterward in good faith gives the debtor further credit without security of any kind for property which becomes a part of the debtor's estate, the amount of such new credit remaining unpaid at the time of the adjudication in bankruptcy may be set off against the amount which would otherwise be recoverable from him."

In other words, a preferred creditor who gives further credit is entitled to a setoff. It is impossible to believe that Congress intended that one who gives value originally shall be entitled to nothing except to claim as a general creditor.

Section 70 (d) provides:

> "After bankruptcy and either before adjudication or before a receiver takes possession of the property of the bankrupt, whichever first occurs:—
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> (1) A transfer of any of the property of the bankrupt, other than real estate, made to a person acting in good faith shall be valid against the trustee if made for a present fair equivalent value or, if not made for a present fair equivalent value, then to the extent of the present consideration actually paid therefor, for which amount the transferee shall have a lien upon the property so transferred;" Act of June 22, 1938, C. 575, Sec. 1, 52 Stat. 879, 11 U. S. C. A. Sec. 110.

Under this Section a bankrupt, *after* bankruptcy, may make a transfer to a person acting in good faith, and such transfer will be protected to the extent of the present consideration given therefor. It is absurd to suppose that Congress intended to place transactions for a present consideration prior to bankruptcy in a less advantageous position than those made after bankruptcy and yet the result of the decision of the Circuit Court of Appeals in the present case is that what may be properly done after bankruptcy may not be done before. As stated by Mr. Neuhoff in his able article "Assignments of Accounts Receivable as Affected by the Chandler Act" in *34 Ill. L. Rev.* 538, 544 (1940):

> "While it would be legally possible for Congress so to provide, the difficulty in justifying such disparity of treatment on any logical theory leads very forcibly to the conclusion that Congress had no such intention."[1]

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[1] See also *4 Remington on Bankruptcy* (4th Ed.) Sec. 1717; *Hamilton, The Effect of Section 60 of the Bankruptcy Act upon Assignments of Accounts Receivable,* 26 Va. L.

It is clear that where value is given time is wholly unimportant. If there is any distinction at all, it is in favor of the validity of transactions occurring prior to bankruptcy. As we all know, one of the purposes of the Bankruptcy Act is to encourage, not to defeat, the giving of credit to those in financial difficulties in the hope that they may be surmounted. This was well expressed by Mr. Justice Davis in *Tiffany v. Boatman's Institution*, 85 U. S. 375 (1873), where he said (p. 388):

> "And it makes no difference that the lender had good reason to believe the borrower to be insolvent if the loan was made in good faith, without any intention to defeat the provisions of the Bankrupt Act. It is not difficult to see that in a season of pressure the power to raise ready money may be of immense value to a man in embarrassed circumstances. With it he might be saved from bankruptcy, and without it financial ruin would be inevitable. If the struggle to continue his business be an honest one, and not for the fraudulent purpose of diminishing his assets, it is not only not forbidden, but is commendable, for every one is interested that his business should be preserved. In the nature of things he cannot borrow money without giving security for its repayment, and this security is usually in the shape of collaterals. Neither the terms nor policy of the Bankrupt Act are violated if these collaterals be taken *at the time* the debt is incurred. His estate is not impaired or diminished in consequence, as he gets a present equivalent for the securities he pledges for the repayment of the money borrowed. Nor in doing this does he prefer one creditor over another, which it is one of the great objects of the Bank-

Rev. 168 (1939); *Kach, Transfers of Non-Negotiable Accounts and the Chandler Act*, 46 Commercial L. J. 133 (1941).

rupt law to prevent. *The preference at which this law is directed can only arise in case of an antecedent debt.* To secure such a debt would be a fraud on the act, as it would work an unequal distribution of the bankrupt's property, and, therefore, the debtor and creditor are alike prohibited from giving or receiving any security whatever for a debt already incurred if the creditor had good reason to believe the debtor to be insolvent. But the giving securities *when* the debt is created is not within the law, and if the transaction be free from fraud in fact, the party who loans the money can retain them until the debt is paid.". (Emphasis supplied.)

Of course, the Tiffany case arose under the old Bankruptcy Act of 1867 (14 Stat. 517). The purposes of that Act were however the same as those of the present law and the principles of the Tiffany case have never been modified or reversed. To the same effect is the statement of Mr. Justice Brandeis in the case of *Dean v. Davis*, 242 U. S. 438 (1917), where he said (p. 443):

> "The mortgage was not voidable as a preference under § 60b. Preference implies paying or securing a pre-existing debt of a person preferred."

(p. 444):

> "The mortgage may be made in the expectation that thereby the debtor will extricate himself from a particular difficulty and be enabled to promote the interest of all other creditors by continuing his business."

That is exactly the situation which we have in this case. Quaker City Sheet Metal Company was enabled by reason of the advances made to it by the petitioners, to carry on

its business and meet its payroll from May, 1938 until April, 1940 (R. 18, 29, 30, 32, 34).

That Congress should have intended such a complete and revolutionary change in the very fundamentals of the Bankruptcy Law cannot be imputed to it in the absence of a clear showing that the question was called to its attention and that it acted upon it with its eyes open. As Mr. Neuhoff puts it (34 *Ill. L. Rev.* 544):

> "If it is to be converted into a preference by legal legerdemain, the minimum requirement should be that the intention of Congress so to do shall be clearly expressed and not be based upon an obscure 'cross reference.'"

We have examined the Report of the Congressional debates and there is nothing in them, nor in the Report made by Mr. Chandler to Congress, which indicates that Congress had such an intention. See Report No. 1409, on H. R. 8046, July 29, 1937, 75th Congress, 1st Session; 14 Ohio Law Reporter 168.

The Chandler Act further amended the Bankruptcy Act by removing therefrom subsection (d) of Section 67, which provided as follows (11 U. S. C. A. Sec. 107 (d)):

> "Liens given or accepted in good faith and not in contemplation of or in fraud upon the provisions of this title, and for a present consideration, which have been recorded according to law, if record thereof was necessary in order to impart notice, shall, to the extent of such present consideration only, not be affected by anything herein.": Act of June 25, 1910, c. 412, Sec. 12, 36 Stat. 842.

It is clear that this Section was omitted because the amendments to Section 60 (a) made this Section 67 (d)

no longer necessary. Prior to the 1938 amendment of Section 60 (a) the definition of a preference had not contained the words "for or on account of an antecedent debt". See Appendix. By the inclusion of these words in the 1938 amendment the clear intention was to provide that a transfer should only be a preference if the consideration therefor was an antecedent debt. In other words, by so stating in Section 60 (a), it became unnecessary to state the same thing in reverse, i. e., that liens given for a present consideration shall be valid. As explained in the House Committee Report No. 1409, above referred to, the purpose was "to eliminate the overlapping, discard the present cumbersome phrasing, and state the test more accurately, scientifically and comprehensively".

The Decisions.

All of the cases which an exhaustive search has been able to discover support the position of the petitioners. The principal case is that of *Adams v. City Bank & Trust Co.*, 115 F. (2d) 453, 134 A. L. R. 1215 (decided by the Circuit Court of Appeals for the Fifth Circuit in 1940). In that case the bankrupt had given a bill of sale covering personal property to secure an indebtedness simultaneously created. This bill of sale was not recorded until a time when the debtor was insolvent, which time was within four months of bankruptcy, when the creditor had reason to believe that the bankrupt was insolvent. The District Court held that there was no preference within Section 60 (a) of the Bankruptcy Act as amended in 1938, and the Circuit Court of Appeals affirmed this decision, saying, page 454:

> "Prior to the Chandler Act, it was universally recognized that there was no preference, unless there was

a diminution of the estate by reason of the transfer. The preference at which the law was directed could only arise in case of an antecedent debt.

* * * *

It is argued that the Chandler Act has changed the former rule by providing that a transfer shall be deemed to have been made at the time when it became so far perfected that no bona fide purchaser from the debtor and no creditor could thereafter have acquired any rights in the property so transferred superior to the rights of the transferee therein, and that, if such transfer is not so perfected prior to the filing of the petition in bankruptcy, it shall be deemed to have been made immediately before bankruptcy. This argument fails to give due weight to the first sentence of section 60, sub. a, of said act, which provides that a preference is a transfer of the property of a debtor 'for or on account of an antecedent debt.' This refers to the whole transaction, and not simply to the step to be taken to make it binding as to subsequent creditors and purchasers for a valuable consideration. . . .

Our conclusion is that section 60 does not apply to a transfer entered into without fraudulent intent, for an adequate present consideration. In the instant case, the bills of sale were given for a present equivalent at the time the debts were incurred, and did not become preferences voidable in bankruptcy by reason of subsequent filing for record, while the debtor was insolvent, less than four months before the time of bankruptcy." (Emphasis supplied.)

This Court denied certiorari, 312 U. S. 699.

In *Girard v. Kimbell Milling Co.*, 116 F. (2d) 999 (C. C. A. 5, 1941), the same Court followed its earlier decision in the Adams case, saying (p. 1001):

"There was never an unsecured debt, and without that there could be no preference."

Again, in the case of *In re Talbot Canning Corp.*, 35 F. S. 680 (U. S. D. C., Md., 1940) it was held that Section 60 (a) applies only to transfers given for antecedent debts. In that case the Talbot Company had a contract with Sisk & Sons, whereby the latter was to provide it with cans for its business and to sell its products on commission. The Talbot Company purchased its raw materials from Associated Seed Growers, Inc. Seed Growers became dissatisfied with the financial condition of the Talbot Company and demanded security before shipping more merchandise. Accordingly, the Talbot Company assigned to the Seed Growers certain moneys due or to become due from Sisk & Sons on account of finished canned goods which Sisk & Sons either had sold or was selling for the Talbot Company. The Referee held that this assignment constituted a preference under Section 60 (a) of the Bankruptcy Act. The District Court reversed, saying (p. 685):

> "Prior to the amendment of the Bankruptcy Act in 1938, the rule in effect in this Circuit was that equitable liens given for antecedent debts, if created before the four months' period preceding bankruptcy, were valid and enforceable against the trustee in bankruptcy, and were not voidable as preferential even though the funds upon which such liens were a charge, were collected within such four months' period, or even after an adjudication in bankruptcy."

The Court then recited the new provisions incorporated in the Bankruptcy Act of 1938 and held that if the assignments were not given for antecedent debts they were good as against the trustee in bankruptcy, saying (p. 687):

> "If they were not so given, but were given for new purchases in good faith, then, although as we have

seen, the old provision of the Bankruptcy Act expressly protecting such transfers to the extent of the present consideration has been omitted in the new Act, it is not to be inferred from this omission that transfers for present consideration are now brought within the purview of voidable preferences. The inference is just the contrary, *for if value has been given there has been no depletion of the bankrupt's estate and hence no preference.* The definition of a preferential transfer in section 60, sub. a, of the new Act is confined to a transfer given 'for or on account of an antecedent debt,' and under section 60, sub. b, bona fide purchasers for present consideration from a preferred creditor are expressly protected; as is also the preferred creditor under Section 60, sub. c,—which remains as it was before the amendments of 1938,—by way of setoff, to the extent that he may have given new credit in good faith to the bankrupt." (Emphasis supplied.)

The case was remitted to the referee to determine whether or not the assignment was made for an antecedent debt, and, if so, whether or not the assignee had reasonable cause to believe that the bankrupt was then insolvent. The referee found that the assignee did have reasonable cause to believe that the bankrupt was insolvent at the time of the assignment but that the assignment having been for a present consideration, it was not voidable by the trustee in bankruptcy. Upon a second appeal to the District Court of Maryland, 39 F. S. 858 (1941), that Court found as a fact that the assignment had been for an antecedent debt and therefore reversed the referee. The case was then appealed to the Circuit Court of Appeals for the Fourth Circuit under the title of *Associated Seed Growers, Inc. v. Geib*, 125 F. (2d) 683 (1942). The Circuit Court of Appeals for the Fourth Circuit reversed the District Court upon the

ground that it had been in error in finding that the assignment was for an antecedent debt, saying (p. 685):

> "In short, *the assignment was not given for an antecedent debt* but for a present consideration, and since Seed Growers complied with the new contract by shipping the goods, it is entitled to the benefit of the assignment if the assignment is otherwise valid.
>
> *It follows that an essential element of a voidable preference, defined in Section 60, sub. a of the Bankruptcy Act, 11 U. S. C. A. § 96, sub. a, is missing;* and hence the second question listed above" (i. e., whether the assignments constituted voidable preferences under the Bankruptcy Act) "should have been decided in the claimant's favor." (Emphasis supplied.)

The same conclusion was reached in *In Re E. H. Webb Grocery Co.*, 32 F. S. 3 (U. S. D. C., Tenn., 1940). In that case the Court held that the proper interpretation of Section 60(a) disregards the fact that a transfer is only recorded within the four months' period in cases in which the transfer is for a present consideration and does not deplete the bankrupt estate. The District Court, reversing the Referee, said (pp. 4, 5):

> "It is my idea that the Referee has misconstrued this section of the statute. I think that this section of the statute did not change in substance the prior law but simply clarified the former provisions.
>
> Under the facts as stated, I think unquestionably that the mortgage created a lien in favor of the Hooper Grocery Company on September 15, 1938. That is, a lien good between the parties.
>
> Under the Tennessee statutes and authorities, a lien created by a mortgage, unregistered, is good between the parties and is good against everyone except

lien or judgment creditors. When the mortgage is registered it relates back to the date of its execution and is good as of that date as against everyone except lien or judgment creditors.

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I am of the opinion that this transfer was perfected on September 15, 1938, which was more than four months before bankruptcy. I think it was for a valuable consideration, in good faith, did not deplete the estate and was not for an antecedent debt."

It is interesting to note that in the Webb case the mortgage was made on September 15, 1938, and recorded the next day, September 16th, whereas the bankruptcy occurred on January 16, 1939. Hence, had the Court adopted the view of the majority of the Court below in the case at bar, the mortgage would have been within the four months' period and voidable by the trustee in bankruptcy. As a practical matter, a very large percentage of deeds and mortgages are not recorded until a day or two after they are given, either because the Recorder's Office is closed for the day or the document has to be sent to another County for record. Should the decision in the case at bar be sustained, all such transactions, even though given for a present consideration, will be voidable if the recording is within the four months' period. Similarly, where accounts receivable are assigned, anywhere from one to several days will ordinarily elapse between the date of the assignment and the giving of notice by the assignee to the person owing the assigned debt, depending upon their respective geographical locations. Consequently, in States which require such notice, in order to make the assignment good against the world it would not be safe for the lender to actually make the loan until after he had given such notice and received

an acknowledgment. The result in each case would be to complicate all such transactions and make necessary a change in common business practices which have been in effect for years. It is hardly likely that Congress intended the amendment of Section 60 (a) to have any such effect.

The Opinions in the Court Below.

The majority of the Circuit Court of Appeals in its opinion in the case at bar states (R. 43):

> "The rule which the second sentence of subdivision a lays down as to the time when a transfer is to be deemed to have been made is stated, to be 'for the purposes of subdivision a,' inter alia. It is thus clear that the rule is intended to apply to the provisions of the first sentence of that subdivision insofar as they involved questions having to do with the time of making a transfer. There is no indication that its application to the first sentence is to be restricted to the mere determination of whether a transfer is made while the debtor is insolvent and within four months of bankruptcy. On the contrary it is obvious that the time of the making of a transfer is the essential element in determining whether a debt on account of which it is made was antecedent to it."

We submit that in reaching this conclusion the Circuit Court of Appeals overlooked the fact that there is no occasion at all to apply the rule with respect to when a preferential transfer may be set aside, unless you have a preference to start with. The Court is confusing two entirely different things. The first sentence of Section 60 (a) which defines a preference, expressly provides that it is a transfer for an antecedent debt. The second sentence is not an enlargement of the meaning of the term "antecedent debt" used in the definition contained in the first sentence. On

the contrary, it is merely a formula to ascertain whether a transfer for a factual antecedent debt shall be deemed to have been made within four months of bankruptcy. The conclusion of the Court below can only be reached by using the formula for the application of the definition to change the plain stated meaning of the definition itself.

We are unable to improve upon the summary of our position given by Judge Jones in his dissenting opinion in the Court below (R. 47-49):

> "And so, according to the prevailing argument, the entire transaction of contemporaneous loan and transfer is split apart and the unperfected[3] transfer is 'deemed to have been made immediately before bankruptcy', as Sec. 60 (a) provides, while the loan for which the transfer was contemporaneously made retains the original date of the actual transaction and thus becomes antecedent in relation to the time of the transfer, as statutorily presumed under the attending circumstances. To so hold seems to be a striking instance of lifting oneself by one's bootstraps and terminates in a result which I do not think Sec. 60 (a) was intended to bring about. When the time of the transfer is brought to 'immediately before bankruptcy' by virtue of Sec. 60 (a) because of a want of perfec-

[3] The term 'unperfected' as used herein should not be taken to imply that the assignments in this case were wanting in legal validity. Under local law they were binding and conclusive as to the assignor and its creditors from the time they were made. See Phillips's Estate (No. 4), 295 Pa. 525, 531. They were, moreover, good against the world except that a subsequent bona fide purchaser without notice could have acquired rights in the assigned accounts superior to the rights of the original assignees if he was first to give notice of his acquisition to the persons owing the accounts. It was only to that limited extent that there was any want of perfection in the transfers.

tion thereof as against a bona fide purchaser and creditors of the transferor, the fact as to whether the unperfected transfer was for an antecedent debt or for a debt contemporaneously incurred is still to be reckoned with on the basis of actuality. It will be observed that Sec. 60 (a) does not strike down an unperfected transfer but merely moves, by legal presumption, the time of its occurrence to 'immediately before bankruptcy'.

In my opinion, the provision in Sec. 60 (a) with respect to the presumed time of transfer under the specified conditions was incorporated in the Chandler Act in order to bring constructively within the four months of bankruptcy (and thus render adjudicable on that basis) all unperfected transfers made while the debtor was insolvent more than four months prior to bankruptcy. Before the Chandler Act, the law did not reach such earlier transfers by an insolvent debtor. But under Sec. 60 (a), as now amended, any unperfected transfer by an insolvent can be assailed as a preference if, when actually made, the consideration therefor was an antecedent debt. So construed, the provision in Sec. 60 (a), relating to the legally presumed time of transfer, works an important change in the law but it has nothing to do with determining the relative date of the incurrence of the debt for which an unperfected transfer was contemporaneously made. *Whether the unperfected transfer, when made, was made on account of an antecedent debt or for a present consideration of full money's worth remains the criterion for determining whether the transfer constituted a preference.*

What the bankruptcy law is primarily concerned with is the equitable distribution of a bankrupt's estate among creditors. A preference is the favoritism by an insolvent debtor of one creditor over others.[4]

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[4] 3 Collier on Bankruptcy (14th ed.) par. 60.02, pp. 750-751.

But, in order that a payment or transfer by a debtor to one creditor may amount to a preference, it is necessary that the debtor's estate be thereby depleted so that the remaining creditors cannot ratably receive commensurate shares on account of their claims.[5] A transfer therefore which does not reduce the value of a debtor's estate because he contemporaneously receives full value in exchange is not a preference. It is hardly likely that Congress intended by bringing an unperfected transfer to 'immediately before bankruptcy' to constitute a preference out of a transaction which in no way depleted the debtor's estate. Bankruptcy does not disapprove of an insolvent debtor's giving security, even down to the date of bankruptcy, for a present loan of full value. Such action may possibly sustain the breath of fiscal life in a gasping debtor until complete recovery to the ultimate benefit of creditors generally. Indeed, it was in furtherance of that hope that the subject loans in the instant case were given and the transfers made as security therefor. The debtor's estate was in no way depleted but received a needed and desired present benefit. In any view, a contemporaneous transfer in such circumstances is no more a preference under the Chandler Act amendment of Section 60 (a) than it was prior to the amendment." (Emphasis supplied.)

As suggested in the above quotation from the opinion of Judge Jones, the granting of the loans and the assignment of accounts receivable was one transaction. The Courts have so held on several occasions. See *Bridgers v. Hart*, 200 N. C. 685, 158 S. E. 242 (1931); *In Re Perpall*, 271 Fed. 466 (C. C. A. 2, 1921); *In Re Metropolitan Dairy*

[5] See Newport Bank v. Herkeimef Bank, 225 U. S. 178, 184; also 3 Collier on Bankruptcy (14th Ed.) par. 66.19, p. 819.

Company, 224 Fed. 444 (C. C. A. 2, 1915); *In re E. H. Webb Grocery Co.*, 32 F. S. 3, supra. If the fiction in the second sentence of Section 60 (a) is to be applied to move forward the date of the assignment, it must apply equally to the date of the loan. The transaction cannot be split so as to treat the loan as having been made upon its actual date and at the same time move up the date of the assignment in consideration whereof the loan was contemporaneously made.

No Secret Lien in This Case.

It is said by the majority of the Court below (R. 44) that the purpose of the Chandler Act amendment to Section 60 (a) was to strike down secret liens even though given for a present consideration. The effect of the interpretation of the majority of the Court below is to strike down secret and open liens alike. If the petitioners had given notice to the persons owing the assigned accounts, how would that have made the claims of the petitioners any less secret so far as a subsequent assignee was concerned? If such assignee would not take the trouble to look at the books of the assignor where he would have seen the assignments plainly noted, would he be any more likely to write to the persons owing the assigned accounts and ask them if they had had notice of an assignment? Again we quote from the dissenting opinion of Judge Jones below (R. 50) where he said:

> "Nor am I able to see how Sec. 60 (a) was intended, as the majority suggest, 'to strike down secret liens even though given for a present consideration'. The time of the making of a secret lien, if perfected

under local law, is no more deemed to have been 'immediately before bankruptcy' than is the time of the making of a perfected open lien. And, by the same token, an unperfected open lien is subject to the same limitation under Sec. 60 (a) as is an unperfected secret lien. In no sense does Sec. 60 (a) seek to discriminate between secret and open liens. It simply prescribes the requisites under the bankruptcy law for determining the existence of a preferential transfer. And this, it does without attempting in any way to pass disapprovingly upon what may be a valid (although secret) lien under local law."

The facts of the present case furnish an excellent example of the effect of the decision of the Circuit Court of Appeals on liens which are not secret, for there was certainly nothing secret about the liens of the Petitioners. The great majority of the unsecured creditors, now represented by the Trustee in Bankruptcy, knew all about them. Before the loans were made the matter was submitted to representatives of the five principal creditors, who after referring the matter back to their respective Home Offices, entered into an agreement subordinating their claims to new liabilities assumed by the Quaker City Company (R. 7, 8, 27). A Creditors' Committee was appointed, to whom the Quaker City Company agreed to give weekly statements showing all transactions and that the Committee might at any time examine its books (R. 7, 8). The Committee countersigned all checks, executed the assignments to the Bank, signed the notes to the Bank and supervised the business (R. 29-30). The Quaker City Company made notations of the assignments upon its invoices and stamped on its ledger sheets the following legend:

> "For value received this account has been assigned to the Corn Exchange National Bank and Trust Company."

or words to that effect (R. 28).[1]

It is interesting to note that the procedure followed in this case is exactly that which has since been adopted by the Pennsylvania Act of July 31, 1941, P. L. 606 (69 Purdon's Pennsylvania Statutes, Ann., sec. 561), which provides that where the books of the assignor of accounts receivable disclose their assignment, then such assignments shall be valid against all subsequent purchasers, pledgees, creditors, etc., notwithstanding the fact that notice has not been given to the persons owing the accounts receivable. The obvious reason for this change in the Pennsylvania law is that the place to look for an assignment of accounts receivable is on the books of the assignor.

The Status of the Trustee in Bankruptcy.

It was contended by our opponents in the Court below that by Section 60, as now amended, the trustee in bankruptcy has been given a new status, namely, that of a bona fide purchaser. The simple answer to this suggestion is that if there had been any such intention, it would have been so stated in the Sections of the Act which define the status of the trustee. This is covered by Section 70 (a), the first sentence of which provides:

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[1] It has been held in several cases that under such circumstances there can be no bona fide purchaser for the reason that the failure of an assignee to examine books of the assignor prevents the assignee from having such status. See *In Re Johnson-Maas Company*, 45 A. B. R. (N. S.) 32 (1939); *In Re Leader Furniture Company*, 36 Fed. Supp. 986 (U. S. D. C., E. D. Pa. 1939).

> "The trustee of the estate of a bankrupt . . . shall . . . be vested by operation of law with the title of the bankrupt as of the date of the filing of the petition in bankruptcy."[2]

It does not vest in him the rights of a purchaser for value and under the law of Pennsylvania, the title of a bankrupt is only to the equity in the assigned accounts after the discharge of the debts for which they have been pledged as collateral. *Phillips' Estate* (No. 4), 205 Pa. 525, 55 Atl. 216 (1903).

In those States, of which Pennsylvania prior to the Act of 1941 was an example, which have adopted the English rule laid down in the case of *Dearle v. Hall*, 3 Russ. 1, affirmed 3 Russ. 48, 38 Eng. Repr. 475, 492 (1827), to the effect that a second assignee who gives notice is preferred over a prior assignee who has failed to do so, the basis of the rule is not the failure of the first assignee to get good title but an equitable estoppel against him because by failing to give notice he has permitted the assignor to commit a fraud on the second assignee. The rule is not for the benefit of creditors generally. *Shepherd v. Penna. R. R. Co.*, 29 Pa. Superior Ct. 291 (1905). Certainly, it cannot have been the intention of Congress to displace the first assignee in favor of a trustee in bankruptcy, who is not a purchaser for value but, upon the contrary, stands in the shoes of the general creditors. To do so would be to give the trustee in bankruptcy an equity to which only a bona fide purchaser could be entitled, when in fact no bona fide purchaser exists and, if he did, his rights would be supe-

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[2] Act of June 22, 1938, c. 575, Sec. 1, 52 Stat. 879, 11 U. S. C. A. Sec. 110; see also Sec. 70 (c) idem, which gives to the trustee the rights of certain creditors only.

rior to those of the trustee in bankruptcy so that the latter would get nothing, a strange result indeed.

The Importance of the Question Involved.

The Court will take judicial notice of the fact that the lending of money upon assigned accounts receivable is one of the commonest and most important branches of the business of the commercial banks of the country. Many thousands of such transactions involving untold millions, take place each year. It is the little fellow with insufficient working capital, who must finance himself through his accounts receivable, who will be hurt the most by this decision. It is one of the principal ways in which business men obtain money with which to run their businesses. If the banks may not rely with confidence upon such security, one of the greatest sources of credit in the country will be cut off. In the year 1940 the volume of financing secured by the assignment of accounts receivable reached the astounding total of almost two billion dollars. *Saunier & Jacoby, Accounts Receivable Financing* (National Bureau of Economic Research). In the case of *In the Matter of Johnson-Maas Company*, 45 A. B. R. (N. S.) 32 (1939), it appeared from returns to a questionnaire sent out by the Department of Financial Institutions of the State of Indiana, that the banks of that State alone during the year 1938 made over 15,000 loans secured by assigned accounts for a total sum of approximately $19,500,000. The bearing of the question upon the financing of war contracts is obvious. One such case has been brought to our attention where a single loan of $10,000,000 has been held up because of the doubt cast upon its validity by the decision of the Court below. It is incredible that Congress, without discussion and without specific consideration of the point, in-

tended so revolutionary a change in this country's business and financial structure as to do away with this type of loan.

As any business man knows, it is generally impractical to give notice of the assignment to the persons owing the assigned accounts. The concern owing the account generally has a running account with the assignor, consisting of numerous items of debit and credit, and makes payment of a number of invoices in one remittance. If specific accounts were assigned to various people who then gave notice of their respective assignments, the debtor would not know how much he is to pay to each; that is, how the discounts and other credits were to be apportioned between them. This is likely to be harmful to the business of the assignor, as his customer would prefer to deal with him alone. On the other hand, the rights of the assignor and assignee as between themselves are easily adjusted. Consequently, the usual business practice is not to give such notice. This is recognized and is the underlying reason for the Act of 1941 of the Pennsylvania Legislature above referred to, making such assignments valid against the world without the necessity of notice to the persons owing the assigned accounts.

It will be noted that the second sentence of Section 60 (a) does not prescribe any territorial limits for the purpose of determining whether "no bona fide purchaser from the debtor and no creditor could thereafter have acquired any rights in the property so transferred superior to the rights of the transferee therein". Under the interpretation of the Court below, it logically follows that if by the law of any jurisdiction in the United States or elsewhere a bona fide purchaser or a creditor could acquire rights superior to those of the assignee, the security will be destroyed. Obviously, it would be impossible for the lender

to determine with any certainty whether or not this might happen. If, for example, a borrower assigns an account receivable as security for a present loan in a State in which the law does not require notice to the debtor and the borrower later goes into another State where notice is required and there makes a second assignment of the same account receivable, and the second assignee gives notice, such second assignee may well secure a right superior to that of the first assignee. Again, if a man living in New York should give a chattel mortgage upon some article as security for a contemporaneous loan, which chattel mortgage is recorded in accordance with the New York law, and the borrower later removes the chattel across the State line into Pennsylvania, where chattel mortgages are not recognized, and there sells the article, the buyer under the law of Pennsylvania would acquire a better title to it than the lender in New York. Consequently, the possibility that this might happen would invalidate the chattel mortgage in the event of the bankruptcy of the borrower.

Deeds and mortgages recorded within four months of bankruptcy, regardless of when they were given and of the fact that they were given for a present consideration, would be voidable in bankruptcy by the trustee simply because by the failure of the grantee or mortgagee to record at an earlier date, a bona fide purchaser from the grantor or a bona fide lender to the mortgagor might have secured a superior title, although in fact this never occurred.

It is clear that the question involved is one of the greatest importance to the business life of the country. The assignments here in question were taken for a present consideration, i. e., when the money was paid, so that there was no depletion of the bankrupt's estate. No artificial rule can alter that fact. Under a proper interpretation of

Section 60 (a), no assignment can be a preference if it is given for a present consideration. There must be an unsecured debt at some time or there can never be a preference. The second sentence of Section 60 (a) is only intended to determine when an assignment *for some antecedent debt* becomes perfected for the purpose of the four months' rule and is wholly inapplicable to the facts of this case.

It is therefore respectfully submitted that the decision of the Circuit Court of Appeals should be reversed.

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APPENDIX.

Bankruptcy Act, approved July 1, 1898, c. 541, 30 Stat. 562:

Sec. 60. Preferred Creditors.—(a) A person shall be deemed to have given a preference if, being insolvent, he has procured or suffered a judgment to be entered against himself in favor of any person, or made a transfer of any of his property, *and the effect of the enforcement of such judgment or transfer will be to enable any one of his creditors to obtain a greater percentage of his debt than any other of such creditors of the same class.*

Amendment approved February 5, 1903, c. 487, 32 Stat. 799:

Sec. 13. That subdivisions a and b of section sixty of said Act be, and the same are hereby amended so as to read as follows:

"(a) A person shall be deemed to have given a preference if, being insolvent, he has, within four months before the filing of the petition, or after the filing of the petition and before the adjudication, procured or suffered a judgment to be entered against himself in favor of any person, or made a transfer of any of his property; *and the effect of the enforcement of such judgment or transfer will be to enable any one of his creditors to obtain a greater percentage of his debt than any other of such creditors of the same class.* Where the preference consists in a transfer, such period of four months shall not expire until four months after the date of the recording or registering of the transfer, if by law such recording or registering is required."

Amendment approved June 25, 1910, c. 412, 36 Stat. 842:

Section 11. That section sixty, subdivision b, of said Act as so amended be, and the same hereby is, amended, so as to read as follows:

"If a bankrupt shall have procured or suffered a judgment to be entered against him in favor of any person or have made a transfer of any of his property, and if, at the time of the transfer, or of the entry of the judgment, or of the recording or registering of the transfer if by law recording or registering thereof is required, and being within four months before the filing of the petition in bankruptcy or after the filing thereof and before the adjudication, the bankrupt be insolvent and the judgment or transfer then operate as a preference, and the person receiving it or to be benefited thereby, or his agent acting therein, shall then have reasonable cause to believe that the enforcement of such judgment or transfer would effect a preference, it shall be voidable by the trustee and he may recover the property or its value from such person. And for the purpose of such recovery any court of bankruptcy, as hereinbefore defined, and any state court which would have had jurisdiction if bankruptcy had not intervened, shall have concurrent jurisdiction."

Amendment approved May 27, 1926, c. 406, 44 Stat. 666:

Sec. 14. That section 60 (a), of said Act as so amended, be, and the same hereby is, amended to read as follows:

"(a) A person shall be deemed to have given a preference if, being insolvent, he has, within four months before the filing of the petition, or after the filing of the petition and before the adjudication, procured or suffered a judgment to be entered against himself in favor of any person, or made a transfer to any

of his property, *and the effect of the enforcement of such judgment or transfer will be to enable any one of his creditors to obtain a greater percentage of his debt than any other of such creditors of the same class.* Where the preference consists in a transfer, such period of four months shall not expire until four months after the date of recording or registering the transfer, if by law such recording or registering is required or permitted."

Amendment approved June 22, 1938, c. 575; 52 Stat. 869; 11 U. S. C. A. Sec. 96:

Sec. 60. Preferred Creditors.—(a) A preference is a transfer, as defined in this Act, of any of the property of a debtor to or for the benefit of a creditor for or on account of an antecedent debt, made or suffered by such debtor while insolvent and within four months before the filing by or against him of the petition in bankruptcy, or of the original petition under chapter X, XI, XII, or XIII of this Act, *the effect of which transfer will be to enable such creditor to obtain a greater percentage of his debt than some other creditor of the same class.* For the purposes of subdivisions a and b of this section, a transfer shall be deemed to have been made at the time when it became so far perfected that no bona fide purchaser from the debtor and no creditor could thereafter have acquired any rights in the property so transferred superior to the rights of the transferee therein, and, if such transfer is not so perfected prior to the filing of the petition in bankruptcy or of the original petition under chapter X, XI, XII, or XIII, of this Act, it shall be deemed to have been made immediately before bankruptcy.

IN THE

Supreme Court of the United States

October Term, 1942.

No. 452.

CORN EXCHANGE NATIONAL BANK AND TRUST COMPANY, PHILADELPHIA, and EDWARD C. DEARDEN, SR.,

Petitioners,

v.

NORMAN KLAUDER, Trustee of the Estate of QUAKER CITY SHEET METAL CO., Bankrupt,

Respondent.

On Writ of Certiorari to the United States Circuit Court of Appeals for the Third Circuit.

BRIEF FOR RESPONDENT.

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INDEX TO BRIEF FOR RESPONDENT.

TABLE OF CASES CITED.

AUTHORITIES AND REPORT CITED.

STATUTES CITED.

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Respondent.

ON WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE THIRD CIRCUIT.

Brief for Respondent.

Argument.

THE APPLICABLE PENNSYLVANIA RULE.

It is to be observed that by the decision of this Court in *Erie Railroad Company v. Tompkins*, 304 U. S. 64, the unwritten or common law of the state, as declared by its highest court, in the absence of any conflict with the Constitution of the United States or the federal statutes, is binding upon the federal courts whose duty it is to follow it. That decision expressly overruled cases to the contrary, more particularly, *Salem Trust Company v. Manufac-*

turers Finance Company, 264 U. S. 182, and decisions which preceded it.

We have heretofore maintained and the Circuit Court of Appeals has found (Record 44, 45, 46) that the decision of the Supreme Court of Pennsylvania in *Phillips's Estate* (No. 3) 205 Pa. 515, decided in 1903, is controlling. It is therein held that if an assignee of a chose in action fails to give notice to the person holding the fund assigned to him, a subsequent assignee, without notice of the former assignment, will, upon giving notice of his assignment, acquire priority.

In the Circuit Court of Appeals, it was contended by our opponents, as they argue here, that the import of this decision was neutralized by another decision in the same estate rendered by the Supreme Court of Pennsylvania on the same day in *Phillips's Estate*, (No. 4) 205 Pa. 525, in which priority was awarded to an assignee who had not given notice over a subsequent assignee who had given notice. A claimant to a share in a decedent's estate had transferred his interest to successive assignees. The first did not give notice and the second did. In the period intervening between the two assignments a creditor of the claimant attached the fund. The court awarded the creditor priority over the second assignee because the attachment was served prior to the date of the second assignment. The lien of the creditor, however, was subordinated to that of the first assignee. It was held that as between the assignor and the assignee, the assignment was valid with or without notice; that by the attachment, the creditor became an equitable assignee of that which his debtor still had a right to assign, and that as to the creditor, the prior assignment, with or without notice, was valid.

The Circuit Court of Appeals concluded (Record 45) and we submit properly so, that the decision in *Phillips's Estate* (No. 4) involved the determination of the rights of an attaching creditor; that it was based on the theory that an attaching creditor could not secure rights superior to those of a prior assignee even though the latter had not given notice and accordingly held that the decision did not in any way modify the ruling in *Phillips's Estate* (No. 3) with regard to the priority between successive assignees where the first assignee has failed to give notice.

Judge Maris, speaking for the Circuit Court of Appeals, aptly points out, in the majority opinion, that we are here concerned with the rights of purchasers as well as creditors, wherein he states (Record 45):

> "The rule as to the time of making a transfer, which is laid down in the second sentence of Section 60a, cannot operate to fix that time as of the time of actual transfer unless two bases for such operation are present. It must appear to have then been so far perfected that (1) no bonafide purchaser and (2) no creditor could thereafter have acquired superior rights in the property transferred. In the case before us it is immaterial that Phillips's Estate (No. 4), which deals with the rights of creditors, provides one of the bases for the operation of the rule in favor of the date of actual transfer since Phillips's Estate (No. 3), which fixes the rights of purchasers does not provide the other basis. As we have said, the statute requires the presence of both. Consequently if, as here, one is absent, the date of transfer must be deemed to be postponed to the later date fixed by the second sentence of subdivision a, in this case the date of bankruptcy."

STATUTORY DEVELOPMENT OF PREFERENCE DOCTRINE.

A proper approach to the question and a determination of the purpose of the revision of Section 60 of the Bankruptcy Act requires an examination of the history of the legislation. The section has been the subject of several amendments, the purpose of all of which has been to strike down secret transfers executed but not disclosed by recording or change of possession until immediately prior to the bankruptcy of the transferor.

Under the Bankruptcy Act of July 1, 1898, c. 541, Section 60, 30 Stat. 562, 11 U. S. C. A., Sec. 96, Section 60b provided merely that any preference given within four months before bankruptcy might be voidable by the trustee. The section made no provision for cases where recording of a transfer, by state laws, was involved.

The Amendment of February 5, 1903, c. 487, Section 13, 32 Stat. 799, 11 U. S. C. A., Sec. 96 added a provision to Section 60a that "where the preference consists in a transfer, such period of four months shall not expire until four months after the date of recording or registering of the transfer, if by law such recording or registering is required". Following that amendment it was held, however, that the time of recording as distinguished from the date of transfer was not necessarily the test as to its preferential character.

Collier on Bankruptcy, 14th Ed., Vol. 3, page 870.

On June 25, 1910, c. 412 Sec. 11, 36 Stat. 842, 11 U. S. C. A. Sec. 96, the section was further amended so as to provide that the transfer should be voidable "If by law recording or registering thereof is required, and being

within four months before the filing of the petition in bankruptcy—the bankrupt be insolvent and the transfer then operate as a preference" etc. It was thereafter held that a transfer was required to be recorded where, under state law, recording was essential in order to make the transfer valid as against creditors including those whose position the trustee was entitled to take. On the other hand, a transfer was not required to be recorded where, by state law, an unrecorded transfer was void only as against subsequent purchasers for value.

Collier on Bankruptcy, supra, page 870.

At that stage of the law, before a trustee in bankruptcy could avoid a transfer, this Court held that he had to represent in fact or be entitled to take the status of a creditor whose claim actually stood in a superior position to the challenged transfer, while unrecorded and within the specified period. Although there was evidence of legislative intent to determine the preferential nature of a transfer as of the date of recording and the same was given effect by some federal courts, the decisions of this Court in *Bailey v. Baker Ice Machine Co.*, 239 U. S. 268, 35 Amer. B. R. 814, 36 S. Ct. 50, 60 L. Ed. 275, *Carey v. Donohue*, 240 U. S. 430, 36 Amer. B. R. 704, 36 S. Ct. 386, 60 L. Ed. 726 and *Martin v. Commercial National Bank*, 245 U. S. 513, 40 Amer. B. R. 765, 38 S. Ct. 176, 62 L. Ed. 441, settled the controversy. Thus it became established by this Court (1) that a transfer was not required to be recorded or registered where, under applicable state law, an unrecorded transfer was defeasible only as against subsequent purchasers in good faith, (2) that a transfer was required to be recorded where failure to record made the transfer voidable by general creditors, and (3) where recording was required, the preferential

character of the transfer was to be determined as of the date of recording, but if recording was not required determination had to be made as of the date of the transfer itself, not as of the date of recording, nor as of the taking of actual possession under a prior unrecorded transfer. Moreover, before a trustee could successfully avoid a transaction not required to be recorded, but which in fact was recorded or possession taken by the creditor some time prior to bankruptcy, it was necessary that the trustee in fact represent or be entitled to take the place of some creditor whose claim actually stood in a superior position to the challenged transfer. Accordingly, as in the *Martin* case, *supra*, where the state law made an unrecorded conveyance defeasible only as to creditors who, prior to recording, had acquired a lien by attachment or execution and there was actually no such creditor prior to recording, the trustee was not in a position to challenge the transfer, except possibly as a fraudulent conveyance.

Collier on Bankruptcy, supra, pages 873, 874.

By the Act of May 27, 1926, c. 406, Sec. 14, 44 Stat. 666, 11 U. S. C. A. 96, the section was again amended to overcome the effect of unfavorable judicial interpretation by adding the words "or permitted" to the last sentence of Section 60a. It was thereafter held nevertheless that Congress had not effectively changed the definition of a preferential transfer although there were decsions to the contrary.

Collier on Bankruptcy, supra, page 874.

The history of the efforts of Congress from 1903 to 1926 to strike down secret liens by the amendments to Section 60, and the interpretations of the courts thereon are summarized by Judge Lindley of the United States District Court for the Eastern District of Illinois in the matter of

Hirschfeld, Trustee v. Nogle, 5 Fed. Supp. 234; 24 Amer. B. R. (New Series) 363.

Thus the law stood until the amendment of June 22, 1938, c. 575, 52 Stat. 869, 11 U. S. C. A. Sec. 96.

THE CONGRESSIONAL INTENT.

In tracing the history of the changes in Section 60 of the Bankruptcy Act of 1898, we have endeavored to demonstrate a continuing and fairly evident legislative intent to strike down secret transfers by establishing a test as to perfection that fixes the date of notoriety as the time when its preferential character should be determined. It has been said that this intent has been manifest and clear, but that its expression was faulty as a result of which achievements have been weak. Turning to the Amendment of 1938, it is apparent that the draftsmen endeavored to clarify the entire section and to restate it so that a comprehensive test would be afforded for the purpose of reaching all types of secret liens and transfers.

The House Committee in which the amendment was formulated thus states its reasons for rewriting this section. (Report No. 1409 on H. R. 8046, July 29, 1937, 75th Congress, 1st Session):

> "Present Sec. 60a: The language of the present law is cumbersome, and the definition of a preference is not a scientific one. If literally construed, the percentage test may be restricted to the situation existing at the time the transfer is made. Some courts have, in fact, adopted such literal construction. However, the preferential nature of the transfer should be tested rather by the ultimate result, which is the view taken by other courts. The conflict has recently been settled by the Supreme Court in the case of Palmer Clay Products Co. v. Brown (56 S. Ct. 450, 80 L. Ed. 655) in

favor of the retrospective construction. It is thereby deemed advisable to eliminate the overlapping, discard the present cumbersome phrasing, and state the test more accurately, scientifically and comprehensively. Section 60 a as recast accomplishes this desirable result. The new test is more comprehensive and accords with the contemplated purpose of striking down secret liens. It is provided that the transfer shall be deemed to have been made when it became so far perfected that neither a bona fide purchaser nor creditor could thereafter have acquired rights superior to those of the transferee. As thus drafted, it includes a failure to record and any other ground which could be asserted by a bona fide purchaser, or a creditor of the transferor, as against the transferee. A provision also has been added which makes the test effective even though the transfer may never have actually become perfected."

From this language it is certainly logical to assume that it was not the intention of Congress to limit transactions affected to those subject to recording statutes for this was already established by existing law. On the contrary, it is respectfully submitted that the phraseology above quoted in the House Committee Report, evidences a clear intention to extend the scope and application of the section to reach so-called equitable liens which may require perfection or steps essential to a valid transfer at common law.

Doubt has been expressed whether the draftsmen of the act contemplated the result which has been reached in the instant case. Professor James Angell McLaughlin of Harvard University Law School, a member of the National Bankruptcy Conference, which was largely responsible for the drafting of the act, and who is credited with the

phraseology employed in the section under consideration, in his article, "*Aspects of the Chandler Bill to Amend the Bankruptcy Act.*" 40 University of Chicago Law Review 369 (April 1937), at page 393, said:

> "How great a step to take with particular reference to the status of the trustee has been the subject of repeated and extensive debate in the Conference. (National Bankruptcy Conference.)* The Chandler Bill has not embraced the solution perhaps most obviously suggested by the Martin Case (Martin v. Commercial National Bank, 245 U. S. 513)* to give the trustee the status of the holder of a lien antedating bankruptcy by four months. That would give him an undesirable seniority over bona fide transferees. The solution proposed is a simple declaration that for the purpose of avoiding preferences, a 'transfer shall be deemed to have been made at the time when it became so far perfected that no bona fide purchaser from the debtor and no creditor could thereafter have acquired any rights in the property so transferred superior to the rights of the transferee.' It will be observed that by giving the trustee the status of a bona fide purchaser he is brought within the protection of the common real estate recording acts, thus reversing not only the Martin case and like cases but the leading case of Carey v. Donohoe (240 U. S. 430),* which arose on a Georgia real estate statute. Furthermore the phrasing is not limited to secret liens within the recording acts. It is broad enough to cover analogous cases such as those where a judge-made 'equitable lien' is invoked to save secret transfers invalid for failure to take the steps essential to a valid transfer at common law."

It would appear that Professor McLaughlin's article was brought to the attention of the Congressional Commit-

*Inserts ours.

tees when the Bill was under consideration and that there is no doubt as to the intention of the Conference when the Bill was prepared. Professor McLaughlin states further (at page 394):

> "The Bill further has the strength and weakness of a single crisp revision covering a multitude of situations. The 1927 precursor of this paragraph contained, for instance, a separate paragraph upon the topic of floating liens. This paragraph, along with various other attempts to spell out particular situations, was eliminated in the Conference, pursuant to the general theory that the statement of one detail invites another and that bankruptcy laws should not undertake detailed codification concerning business transactions."

Thus it is demonstrated that the purpose of the draftsmen was to develop a test of perfection of transfer that would apply to real and chattel mortgages, conditional sales, trust receipts, equitable liens, assignments and any other type or modes of transfer whereby a creditor obtains security for the obligation owned. It is equally clear that the very essence of the change made in the section is the establishment of the time when the preferential character of the transfer is to be judged. While it is true that the construction reached by the Circuit Court of Appeals here results in the shifting of the time of transfer from the date when the transaction was originally entered into, closer to the date of bankruptcy, this is the very objective of the provision, namely, the striking down of the advantage sought to be gained by secrecy.

It is also to be observed that the amendment simultaneously made to Section 67b of the Bankruptcy Act (Act of June 27, 1938, c. 575, Sec. 1, 52 Stat. 875, 11 U. S. C. A. Sec. 107), is also indicative that Congress had in mind that the

amendment to Section 60 would have the effect which the Circuit Court of Appeals has ascribed to it? Section 67b as so amended, provides:

> "The provisions of section 60 of this Act to the contrary notwithstanding, statutory liens in favor of employees, contractors, mechanics, landlords, or other classes of persons, and statutory liens for taxes and debts owing to the United States or any State or subdivision thereof, created or recognized by the laws of the United States or of any State, may be valid against the trustee, even though arising or perfected while the debtor is insolvent and within four months prior to the filing of the petition in bankruptcy or of the original petition under Chapter X, XI, XII or XIII of this Act by or against him. Where by such laws such liens are required to be perfected and arise but are not perfected before bankruptcy, they may nevertheless be valid, if perfected within the time permitted by and in accordance with the requirements of such laws, except that if such laws require the liens to be perfected by the seizure of property, they shall instead be perfected by filing notice thereof with the court."

This strongly implies that Congress understood that Section 60, as amended, might otherwise have invalidated such liens. Under the law as it stood prior to 1938 and our opponents' contention as to the meaning of Section 60, as now amended, that would seldom, if ever, be true. For illustration, the law prior to the 1938 amendment did not prevent a landlord from securing payment of his rent in full by suing out and levying a distress warrant immediately before bankruptcy—*Henderson v. Mayer*, 225 U. S. 631, 56 L. Ed. 1233. This was so because the distress warrant was held not to create a lien, but merely to perfect an inchoate lien which had previously arisen by operation of the law. If the Petitioners' contention as to the meaning

of Section 60, as amended, be correct and the question as to whether a lien secures an antecedent debt is to be determined as of time when the lien came into existence, rather than as of the time when it was so far perfected as to be good as against bona fide purchasers, Section 60, as amended, will still have little, if any, effect on such liens since practically, they always arise by operation of law simultaneously with the creation of the debt. On the other hand if Section 60 is given the interpretation made by the Circuit Court of Appeals in the instant case, it would invalidate many such liens in the absence of an amendment of Section 67b, so that there was need to amend 67b to except them from its operation.

DISCUSSION OF DECISIONS.

In *Adams v. City Bank and Trust Co.*, 115 Fed. (2d) 453, 44 Amer. B. R. (new series) 196; cited by Petitioners (their brief page 18) the Circuit Court of Appeals for the Fifth Circuit, in construing the amendment, held that the contention which we make here, fails to give due weight to the first sentence of Section 60a, which provides that a preference is a transfer of the property of a debtor "for or on account of an antecedent debt." Thus, that court held that irrespective of the absence of notice, there could not be an antecedent debt if the assignments were made at the time the moneys were loaned and hence the section had no application whatsoever to the situation with which we are here concerned. In other words, it is the ruling of that court that the words "antecedent debt" are the guide by which the language of the entire section must be construed and restricted.

We submit that this decision is contrary to the plain and express language of the statute. Following the defini-

tion of a preference Section 60a recites that "For the purpose of subdivisions a and b of this section, a transfer shall be deemed to have been made etc." This provision does not merely relate to the words "transfer" and "made" appearing in the definition, but on the contrary, is intended to and does qualify the entire definition of a preference including the words "for and on account of an antecedent debt" found in subdivision a. If the monies were advanced and the debt thus created and the transfer or assignment of the accounts, is by the terms of the act, held to have been made at the time of perfection, then, it must necessarily follow that what might have been or intended to be a present consideration, becomes an antecedent debt within the meaning of the statute.

As the Petitioners' brief states (page 19) the same court in *Girard v. Kimbell Milling Co.*, 116 Fed. (2d) 999, followed its earlier decision in the *Adams* case, *supra*.

We submit that the conclusion reached by the Fifth Circuit is wholly predicated upon decisions of this Court prior to the adoption of the 1938 amendment, especially *Carey v. Donohue* and *Martin v. Commercial National Bank, supra*, and is wholly at variance with the manifest object and purpose of the legislation. If this construction be adopted by this Court, no change, however intended or manifested, will have been made in the section. The result will continue to be that where recording is necessary, it can be withheld until a few days prior to bankruptcy, secrecy thus maintained as to the creditors and the transferee will prevail. This is one of the very situations which the amendment was designed to cure and we submit that the language employed is sufficiently clear to warrant the construction reached by the Circuit Court of Appeals in the instant case.

In the matter of Talbot Canning Corporation, 35 Fed. Supp. 680, 44 Amer. B. R. (New Series) 811 (Petitioners' brief page 20), the District Court of the United States for the District of Maryland likewise reached the conclusion that transfers for a present consideration are not, by the language of the amendment, brought within the purview of voidable preferences; taking the position that if value be given, there can be no depletion of the bankrupt's estate and hence no preference; that the definition of a preferential transfer in Section 60 is confined to a transfer given "for or on account of an antecedent debt". We think that this conclusion is similarly erroneous for the reasons heretofore assigned. We respectfully submit that the conclusion of Judge Maris in the instant case is in keeping with the object, purpose and spirit of the amendment where in the majority opinion he said (Record 43):

> "It will be noted that the subdivision comprises two sentences. The first lays down the criteria for determining whether a transfer is preferential. The second sentence provides that for the purposes of subdivision a, inter alia, a transfer shall not be deemed to have been made until it has been perfected as against bona fide purchasers from and creditors of the debtor.
>
> It will be seen that one of the criteria laid down by the first sentence of subdivision a for determining whether a transfer is to be treated as a preference is that it is 'for or on account of an antecedent debt.' The question with which we are primarily concerned in this case involves the meaning of this phrase. The question is this. In determining whether a debt is antecedent to a transfer made on account of it are we to apply the rule laid down in the second sentence as to when a transfer is to be deemed as having been made? In other words, is a debt to be treated as ante-

cedent to a transfer actually made contemporaneously but not perfected as against purchasers and creditors of the debtor until a later time? We think that a fair construction of the statutory language requires an affirmative answer to this question. The rule which the second sentence of subdivision a lays down as to the time when a transfer is to be deemed to have been made is stated, to be 'for the purposes of subdivision a,' inter alia. It is thus clear that the rule is intended to apply to the provisions of the first sentence of that subdivision insofar as they involved questions having to do with the time of making a transfer. There is no indication that its application to the first sentence is to be restricted to the mere determination of whether a transfer is made while the debtor is insolvent and within four months of bankruptcy. On the contrary it is obvious that the time of the making of a transfer is the essential element in determining whether a debt on account of which it is made was antecedent to it.

We conclude that the rule laid down in the second sentence of subdivision a of Section 60 for determining the time of the making of a transfer applies to the determination of the question whether the transfer was made for or on account of an antecedent debt. In this conclusion we are supported by students of the act who have forcefully pointed out that the purpose of Section 60a, as amended by the Chandler Act of 1938, was to strike down secret liens even though given for a present consideration."

As indicated in the Petitioners' brief (page 21), the *Talbot Canning Corporation* case, *supra*, on a second review in the District Court, 39 Fed. Supp. 858, had no bearing on the precise point here involved inasmuch as the District Court found that the transfers complained of were, in fact, made for an antecedent debt. On appeal, however, the

Circuit Court of Appeals for the Fourth Circuit under the name of *Associated Seed Growers, Inc. v. Geib*, 125 Fed. (2d) 683, reversed the District Court; found that the transfers were made for a present consideration and consequently concerned itself with the precise problem here involved. The court held that the validity of the assignment was to be tested by reference to the time when it was made, and if not preferential then, it did not become so because the funds came into the debtor's hands within four months of bankruptcy; predicating its decision upon *Union Trust Company v. Townsend*, 101 Fed. (2d) 903. The court did not concern itself with the history of the legislation nor its object and purpose, at least the reported decision does not so reflect.

In the matter of E. H. Webb Grocery Co., 32 Fed. Supp. 3, 45 Amer. B. R. (New Series) 193 (Petitioners' brief page 22), the Referee had ruled that the mortgage became effective on the date of its registration as distinguished from the time of its execution; that thus the claim was for an antecedent debt. The District Court held, however, that the amendment to Section 60 simply clarified the former provision and again predicated its conclusion on *Martin v. Commercial National Bank, supra*, and that before a trustee may avoid a transfer because of the provisions of Section 60, as amended, he must in fact represent or be entitled to take the place of some creditor whose claim actually stood in a superior position to the challenged transfer, while unrecorded and within the specified period. The court ruled that there had been no substantive change and that the effect, if any, of the statute was simply one of clarification. We submit that this conclusion is erroneous for the reason assigned by Judge Maris in the majority opinion in the case at hand (Record 43).

In *Johnson-Maas Company, Inc., Bankrupt*, 45 Amer. B. R. (New Series) 32, although deciding adversely to the trustee in bankruptcy on the ground that the law of the State of Indiana did not require notice of an assignment or other instrument of transfer to perfect the assignee's title, Referee Wilde, after reciting the provisions of Section 60a and b, said (at page 39):

> "The effect of the above language would seem to be that although an assignment or other instrument of transfer is executed contemporaneously with the making of a loan, if the method or mode of transfer is such that some other creditor could thereafter have acquired any rights in the property transferred by way of security superior to the rights of the original lender, it shall be considered that the transfer was made immediately before bankruptcy, and hence, it must follow, that the transfer was made for or on account of an antecedent debt and would, therefore, be subject to being avoided by the trustee if the person receiving the transfer, at the time the transfer became effective, had reasonable cause to believe that the transferor was insolvent. It would seem, therefore, in the instant case, that the question resolves itself into whether or not a subsequent assignee of the accounts receivable here under consideration could have acquired rights in said accounts, by giving notice to those owing them, superior to the rights of the bank therein. As appears both from the briefs filed on behalf of the trustee in bankruptcy and of the bank, the courts of many states have held that in order to perfect an assignment of accounts, so as to exclude the acquisition of superior rights therein by subsequent assignees, it is necessary to give notice of the assignment to the debtors owing the accounts, the states whose courts have so held including Missouri and Pennsylvania. Such appears also to be the rule in England. In our federal courts

a contrary rule has been adopted. In Salem Trust Company v. Manufacturer's Finance Company, 264 U. S. 182, 68 L. Ed. 628, it was held that mere priority of notice does not give priority of right as between successive assignees of a chose in action. As pointed out, however, by counsel for the trustee in bankruptcy, under the rule followed in Erie Railroad Company v. Tompkins, 304 U. S. 64, — L. Ed. 1188, federal courts look to the law of the state for determination of the substantive law."

THERE WAS A SECRET LIEN.

Judge Jones of the Circuit Court of Appeals who wrote the minority opinion (Record 50) professed an inability to see how the section was intended to strike down secret liens even though given for a present consideration. The Petitioners argue (their brief, 28) "if the petitioners had given notice to the persons owing the assigned accounts, how would that have made the claims of the petitioners any less secret so far as a subsequent assignee was concerned?". The purpose of the amendment to Section 60 is the protection of creditors and to insure equitable distribution of their debtor's assets in the event of his bankruptcy. The inquiry should properly be "how would the failure of the petitioners to give notice of their assignments have made the claims of the petitioners any less secret so far as creditors were concerned?" It cannot be denied that where notice is given, the fact that the debtor has assigned his accounts receivable permeates business channels and invariably results in putting others dealing with him on notice of their debtor's financial condition. The fact that a debtor does assign his accounts receivable is of great importance in the extension of credit. One of the pertinent factors in the written financial statement in common use today relating to businesses, large and small,

bears on the question whether the subject of credit has assigned his accounts receivable and if so, the extent thereof.

The deficiency heretofore existing in the Bankruptcy Act, the results flowing therefrom and the evil sought by the framers of Section 60 to be corrected are best exemplified by *Zehner v. Southern Surety Co.*, 272 Fed. 954, 47 Amer. B. R. 132, a decision of the Circuit Court of Appeals for the Third Circuit in 1921. Over four months prior to its bankruptcy, a road construction company gave to its surety a bill of sale for its machinery and road building equipment. About two months prior to the bankruptcy of the construction company, the surety took physical possession of the property. The case arose in Pennsylvania and in this State, since *Clow v. Woods*, 5 Sergeant & Rawle (Pa.) 275, decided in 1819, it has been the law that a sale of tangible personal property; leaving the vendor in possession and without doing anything to indicate a change of ownership, is fraudulent as against creditors. The result is that when a vendee or pledgee in Pennsylvania takes title to tangible personal property without taking possession of it, he takes the risk of the integrity and solvency of his vendor or pledgor when the rights of subsequent bona fide purchasers or of levying creditors arise. *White v. Gunn*, 205 Pa. 229. Notwithstanding this state law, to which due recognition was given, the Circuit Court, on the authority of *Bailey v. Baker Ice Machine Co., supra*, was obliged to and did hold that under the 1910 amendment of the Bankruptcy Act, the construction company's trustee in bankruptcy could not recover the machinery from the surety as a preference or otherwise. Thus one who has loaned money; has taken as collateral security therefor a bill of sale for all or a greater part of his debtor's

tangible personal property, may maintain the secrecy of the transaction; permit his debtor to remain in possession with all of the indicia of ownership and to incur obligations upon the strength of such apparent ownership and then, when the bankruptcy of his debtor is imminent, step in and possess himself of the property free of the claims of the trustee and of the creditors; where a creditor, prior to bankruptcy, has not actually levied on the personal property pledged.

STATUS OF A TRUSTEE IN BANKRUPTCY.

In order to affirm the decision of the Circuit Court of Appeals it is unnecessary to constitute a trustee in bankruptcy a bona fide purchaser. The rights of a trustee are measured by what is necessary to perfect a transfer, a test or standard rather than a status and it is not essential to adopt an extreme theory which, if applied elsewhere, would work results not intended. The test is drawn so as to direct judicial investigation of the transfer to a time when it has become notorious or publicly known or has lost the aspect of secrecy such as lack of record or change of possession. As stated succinctly by Jacob I. Weinstein, Esquire, of the Philadelphia Bar, one of the draftsmen of the Chandler Act in *The Bankruptcy Law of 1938* (at page 120) it relates to a point of time "when the debtor has done everything required of him under applicable State law in order to make the transfer so complete that it would be good against the whole world."

It is equally clear that the section does not purport to giving a trustee any right or status not elsewhere conferred. To hold otherwise would make Section 60 ludicrous in application.

Collier on Bankruptcy, supra, page 917.

CONCLUSION.

The affirmance of the decision of the Circuit Court of Appeals here will not, as Petitioners complain, hurt the "little fellow" who must finance through the pledge of his accounts receivable; nor will it cut off one of the greatest available sources of credit; nor will it make any less secure the acceptance of such collateral by banks and finance companies. While in the instance shown by the Petitioners (their brief, 33), the giving of notice might in some instances present practical difficulties, there is no sound legal reason why in those states where the law so requires, compliance cannot be had. The desire to conform cannot be attributed to a reluctance on the part of banks and financial institutions to avoid what may be considered an added burden, but rather on the part of the borrower who desires to keep the knowledge of the assignment secret. Why then does the borrower wish to conceal from his creditors the knowledge that he has pledged his accounts receivable? Obviously, because he knows, as heretofore pointed out, that knowledge that he has assigned his accounts will permeate through the channels of the trade and consequently impair his credit. It is generally known that there are large industries in this country, as for example the textile trade, which to a great extent, are financed by factors to whom the accounts receivable of mills are assigned. In that particular industry it is the practice of the factors not only to notify the customer of the mill of the assignment of the account, but to do the actual billing and the collecting of the account as well.

This complaint made now has no merit in Pennsylvania in view of the adoption of the Act of Assembly of July 31, 1941, Pamphlet Laws 606, Title 69, Purdon's Pennsylvania

Statutes Annotated, Sec. 561, which provides that under the circumstances therein outlined, notice of the transfer or assignment of an account receivable need not be given.

The Petitioners would have us believe that the affirmance of the Circuit Court's holding here would destroy or at least seriously affect the credit structure of the country and point particularly to the bearing of the question upon the financing of war contracts. We lean to the view that a clear cut and complete nullification of all types of secret lien transactions would tend to strengthen rather than weaken the general credit structure and prevent circumstances which encourage the unwise extension of credit. To adopt the language of Judge Knapp of the United States Circuit Court of Appeals for the Fourth Circuit in the case of *Brigman v. Covington*, 219 Fed. 500, 33 Amer. B. R. 644 (at page 648), "we believe this is what the Congress intended and with the more confidence because it tends to enforce that open dealing which is the essential basis of commercial morality."

This position, we urge, is consonant with the intent, aim and purpose of the recent Acts of Congress and Executive Orders which are designed to curtail the unwarranted extension of credit and thus to protect and preserve our national economy.

It is respectfully submitted that the decision of the Circuit Court of Appeals should be affirmed.

BERTRAM BENNETT,
HARRY L. JENKINS,
RAWDON LIBBY,
Counsel for Respondent.

SUPREME COURT OF THE UNITED STATES.

No. 452.—October Term, 1942.

Corn Exchange National Bank and Trust Company, Philadelphia, and Edward C. Dearden, Sr., Petitioners,
vs.
Norman Klauder, Trustee of Quaker City Sheet Metal Co., Bankrupt.

On Writ of Certiorari to the United States Circuit Court of Appeals for the Third Circuit.

[March 8, 1943.]

Mr. Justice Jackson delivered the opinion of the Court.

This case requires us to determine the application of the preference provisions of § 60(a) of the Bankruptcy Act as amended by the Chandler Act of June 22, 1938,[1] to loans made on assignments of accounts receivable.

The Quaker City Sheet Metal Company became embarrassed for want of working capital in 1938. Creditors representing a large percentage of claims later proved in bankruptcy agreed to subordinate their claims to those which might be incurred for new working capital. A creditor's committee took supervision of the business and in 1938 arranged with the petitioner Bank to advance from time to time money for payroll and other needs on concurrently made assignments of accounts receivable. At the time of bankruptcy the Company was indebted to the Bank for loans so made on contemporary assignments between January 19, 1940, and April 5, 1940. On April 12, 1940, petitioner Dearden made a loan on similar security. An involuntary petition in bankruptcy was filed against the Company on April 18, 1940, followed by adjudication on May 7, 1940. When the assignments were made they were recorded on the Company's books, but neither petitioner had ever given notice of assignment to the debtors whose obligations had been taken as security. Because of this omission

[1] 52 Stat. 840, 869-870; 11 U. S. C. § 96(a).

the trustee challenged their right to the benefits of their security. He was overruled by the referee and the District Court, but his position was sustained by the Circuit Court of Appeals for the Third Circuit,[2] on an interpretation of § 60(a) which conflicts with an interpretation by the Circuit Court of Appeals for the Fifth Circuit.[3] Hence we granted certiorari.[4]

Section 60(a) as amended and applicable reads:

"A preference is a transfer, as defined in this Act, of any of the property of a debtor to or for the benefit of a creditor for or on account of an antecedent debt, made or suffered by such debtor while insolvent and within four months before the filing by or against him of the petition in bankruptcy, . . . the effect of which transfer will be to enable such creditor to obtain a greater percentage of his debt than some other creditor of the same class. For the purposes of subdivisions a and b of this section, a transfer shall be deemed to have been made at the time when it became so far perfected that no bona-fide purchaser from the debtor and no creditor could thereafter have acquired any rights in the property so transferred superior to the rights of the transferee therein, and, if such transfer is not so perfected prior to the filing of the petition in bankruptcy. . . . it shall be deemed to have been made immediately before bankruptcy."

Section 1(30) specifically provides that "transfer" includes an assignment.[5]

The Circuit Court of Appeals has determined, and we accept its conclusion, that at all relevant times it was the law of Pennsylvania, where these transactions took place, that because of the failure of these assignees to give notice to the debtors whose obligations were taken, a subsequent good-faith assignee, giving such notice, would acquire a right superior to theirs.[6] It held that the assignments were preferences under §.60(a) and therefore, under the terms of § 60(b),[7] inoperative against the trustee.

This is undoubtedly the effect of a literal reading of the Act. Its apparent command is to test the effectiveness of a transfer, as against the trustee, by the standards which applicable state

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[2] 129 F. 2d 894.

[3] Adams v. City Bank & Trust Co., 115 F. 2d 453.

[4] — U. S. —.

[5] 52 Stat. 840, 842, 11 U. S. C. § 1(30).

[6] Phillips's Estate (No. 3), 205 Pa. 515; cf. Phillips's Estate (No. 4) 205 Pa. 525. Pennsylvania has since provided by statute that notice of the assignment on the assignor's books will protect the assignee. Pa. Laws, 1941, No. 255, p. 606 (July 31, 1941), 69 Purd. Stat. Ann. § 561.

[7] 52 Stat. 840, 870, 11 U. S. C. § 96(b).

law[8] would enforce against a good-faith purchaser. Only when such a purchaser is precluded from obtaining superior rights is the trustee so precluded. So long as the transaction is left open to possible intervening rights to such a purchaser, it is vulnerable to the intervening bankruptcy. By thus postponing the effective time of the transfer, the debt, which is effective when actually made, will be made antecedent to the delayed effective date of the transfer and therefore will be made a preferential transfer in law, although in fact made concurrently with the advance of money. In this case the transfers, good between the parties, had never been perfected as against good-faith purchasers by notice to the debtors as the law required, and so the conclusion follows from this reading of the Act that the petitioners lose their security under the preference prohibition of § 60(b).

Such a construction is capable of harsh results,[9] and it is said that it will seriously hamper the business of "non-notification financing," of which the present case is an instance. This business is of large magnitude and it is said to be of particular benefit to small and struggling borrowers.[10] Such consequences may, as petitioners argue, be serious, but we find nothing in Congressional policy which warrants taking this case out of the letter of the Act.

The Committee of the House of Representatives which reported § 60(a) as quoted above was fully aware of the vicissi-

[8] Questions of this sort arising in bankruptcy cases were solved by reference to state law even before the decision of Erie Railroad Co. v. Tompkins, 304 U. S. 64. Holt v. Crucible Steel Co., 224 U. S. 262; Benedict v. Ratner, 268 U. S. 353. The decision in Salem Trust Co. v. Manufacturers' Finance Co., 264 U. S. 182, that, as a matter of "general law," absence of notice to the debtor of the assignment of his account did not open the door to a subsequent assignee to obtain superior rights, was not rendered in a bankruptcy case, and is in any event inapplicable since the decision of the Tompkins case.

[9] Whether the petitioners have any rights under the agreement of some of the creditors to subordinate their claims to those which might be incurred for new working capital is a question which has neither been raised by the parties nor considered by the Court.

[10] Petitioners cite and rely upon Saulnier and Jacoby, Accounts Receivable Financing (National Bureau of Economic Research, 1943), for an estimate that in 1941 commercial finance companies advanced $536,000,000 on this basis; and commercial banks, $952,000,000. Of the borrowers, it was estimated that 63% had total (not net) assets of less than $200,000; and 31%, less than $50,000. Their borrowing was estimated, however, to amount to less than 19% of the total. *Id.* at 17, 32, 64.

"Factoring," a system involving notice to the trade debtors, and confined principally to the textile industry, amounted in 1941 to $1,150,000,000. *Id.* at 3, 17, 58 *et seq.*

tudes of its predecessors.[11] These are recited in detail elsewhere, and need not be repeated here beyond a general statement that for thirty-five years Congress has consistently reached out to strike down secret transfers, and the courts have with equal consistency found its efforts faulty or insufficient to that end.[12] Against such a background § 60(a) was drawn and reported to Congress with this explanation of its purpose and effect: "The new test is more comprehensive and accords with the contemplated purpose of striking down secret liens. It is provided that the transfer shall be deemed to have been made when it has become so far perfected that neither a bona-fide purchaser nor creditor could thereafter have acquired rights superior to those of the transferee. As thus drafted, it includes a failure to record and any other ground which could be asserted by a bona-fide purchaser or a creditor of the transferor, as against the transferee. A provision also has been added which makes the test effective even though the transfer may never have actually become perfected."[13]

Whatever advantages may inhere in non-notification financing which might have made Congress reluctant to jeopardize it, the system also has characteristics which make it impossible for us to conclude that it is to be distinguished from the secret liens Congress was admittedly trying to reach.

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[11] See statement of Professor McLaughlin, Hearings, Revision of the Bankruptcy Act, House Judiciary Committee, 75th Cong., 1st Sess., pp. 122-125. He stated Thompson v. Fairbanks, 196 U. S. 516, as applying a rule of state law that a mortgagee by taking possession of the mortgaged property at a time subsequent to the execution of the mortgage thereby validated it as of the time of execution. He said that § 60(a) would prevent such validation by relation back. Similar disapproving reference was made to Bailey v. Baker Ice Machine Co., 239 U. S. 268; Carey v. Donohue, 240 U. S. 430; and Martin v. Commercial National Bank, 245 U. S. 513; with the explanation that "You are going to have taken away some advantages that some people have enjoyed, and certain practices are going to be altered to some extent. But you have that every time you pass any kind of a commercial law."

[12] See cases cited in the note above; Hirschfeld v. Nogle, 5 Fed. Supp. 234; 3 Collier on Bankruptcy (14th Ed.) §§ 60.05, 60.37. The history and meaning of the present § 60(a) are discussed in 3 Collier, *op. cit. supra*, § 60.48; 2 Glenn, Fraudulent Conveyances and Preferences (1940) § 534; Hanna, Some Unsolved Problems under Section 60A of the Bankruptcy Act, 43 Columbia Law Review 58; McLaughlin, Aspects of the Chandler Bill to Amend the Bankruptcy Act, 4 University of Chicago Law Review 369; Neuhoff, Assignment of Accounts Receivable as Affected by the Chandler Act, 34 Illinois Law Review 538; Mulder, Ambiguities in the Chandler Act, 89 University of Pennsylvania Law Review 10; Hamilton, The Effect of Section Sixty of the Bankruptcy Act upon Assignments of Accounts Receivable, 26 Virginia Law Review 168.

[13] H. R. Rep. No. 1409, 75th Cong., 1st Sess., p. 30.

Receivables often are assigned only when credit in a similar amount is not available through other channels.[14] Interest and other charges are high,[15] and an assignment often is correctly understood as a symptom of financial distress.[16] The borrower does not wish his customers to learn of his borrowing arrangement for the reason, among others, that customers, particularly in placing orders for future delivery, prefer to rely on solvent suppliers. And often the borrower desires to conceal the fact that he is being financed by this method lest knowledge lead to a withdrawal of further credit or refusal of new credit.[17] The borrower and the lender on assigned accounts receivable thus have a mutual interest in not making the transaction known. So long as the transaction may remain a secret, it is not apt to become known to the trade. When the transaction is communicated to the trade debtors it is known where there is less motive to keep it under cover. Commercial and trade reporting agencies are diligent to obtain credit information of this character. Its dissemination may often have adverse effects upon both the borrower and the lender, but they are not the only interested parties. Secrecy has the effect of inducing others to go along with the borrower in ignorance where they would not do so if informed.

It is said that assignments such as are involved in this case could not have been within the contemplation of the Act since its application will have but little effect in remedying whatever secrecy

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[14] Saulnier and Jacoby, *op. cit. supra*, note 10, pp. 6, 21 *et seq.*, 61 *et seq.*

[15] Effective rates are estimated to range from approximately 9% per annum on money in use for the best borrowers to 20% per annum for those whose accounts present the financing company with the heaviest operating costs and whose receivables are of a quality to command only a relatively low percentage advance. *Id.* at 86, 131 *et seq.*

[16] *Id.* at 22, 99.

[17] "Another reason for the use of the non-notification procedure, although less important than other motives and less relevant at present than formerly, seems to have been the desire on the part of the concern being financed to keep the fact of its use of this source of funds from becoming known to its creditors. Presumably these creditors would be less likely to grant the concern further credit on the ground that resort to accounts receivable financing reflected an unsatisfactory financial position and impaired their own security. It seems likely that this attitude toward non-notification financing may be traced to a mixture of simple prejudice and genuine experience with cases where creditors' meetings disclosed for the first time that the bankrupt had secretly assigned his most liquid assets and made unproductive use of the funds so acquired. Genuine experience must have been the more important basis of the two for it its unlikely that an attitude and prejudice so deeply embedded could be founded entirely on misinformation and irrational judgment." *Id.* at 22.

attends them. It is true that notice to the debtors sufficient to satisfy the requirements of applicable state law might never have been communicated to the creditors, and that many states do not require notice to the debtor to foreclose possible superior rights of subsequent assignees.[18] So also is it true that conflicts and confusion may result where the transaction or location of the parties is of such a nature that doubt arises as to which of different state laws is applicable. But the fact that the remedy may fall short in these respects does not justify denying it all effect.

That the assignments in this case were made with the knowledge and acquiescence of many creditors does not cure the failure to meet the requirements of notice laid down by the applicable state law. Neither the words nor the policy of § 60(a) afford any warrant for creating exceptions to fit isolated hard cases.

The judgment below is

Affirmed.

Mr. Justice RUTLEDGE did not participate in the consideration or decision of this case.

Mr. Justice ROBERTS is of opinion that the judgment should be reversed for reasons stated in the dissenting opinion below, 129 F. 2d 897, and in *Adams* v. *City Bank & Trust Co.*, 115 F. 2d 453; *Girard* v. *Kimbell Milling Co.*, 116 F. 2d 999, *In re Talbot Canning Corp.*, 35 F. Supp. 680; *Associated Seed Growers, Inc.* v. *Geib*, 125 F. 2d 683, and *In re E. H. Webb Grocery Co.*, 32 F. Supp. 3.

A true copy.

Test:

Clerk, Supreme Court, U. S.

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[18] See 2 Williston, Contracts (Rev. Ed.) § 435, and Hamilton, *loc. cit. supra*, note 12